85-1368

Supreme Court, U.S.
FILED
FEB 14 1986
JOSEPH F. SPANIOL, JR.
CLERK

No. _____

In the Supreme Court of the United States

October Term, 1985

LAWRENCE J. GALARDI and SHARI J. GALARDI,

Petitioners,

v.

TOKAI BANK OF CALIFORNIA, a California corporation, et al.,

Respondents.

PETITION FOR WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Did the Ninth Circuit erroneously construe the denial of:

A. A jury trial; and

B. A *review* by the District Court,

when it held the issue on appeal below was "first that the exercise of jurisdiction by the Bankruptcy Court was unconstitutional under *Northern Pipeline*. . . ." (Opinion, Appendix A, this Petition.)

2. Were Petitioners deprived of their constitutional right to adjudication of their substantive rights by an Article III Court:

A. When they were denied a jury trial; and

B. When the District Court failed to conduct a review in accordance with the mandate of the Emergency Rule.

3. Did the District Court have the power to appoint a Retired Referee to sit as a Bankruptcy Judge under *Marathon,* under the Emergency Rule, or, any other rule of law.

4. Should the Supreme Court grant certiorari.

PARTIES

Petitioners submit the following list of all persons which have an interest in the outcome of the case before this Court.

Lawrence J. Galardi	Petitioner
Shari J. Galardi	Petitioner
Tokai Bank of California	Respondent
David A. Gill	Respondent

DATED: February 13, 1986

LAWRENCE J. GALARDI
Attorney for Petitioners

TOPICAL INDEX

Statement 1
A. Preliminary 2
B. Factual Summary. The Circumstances Prior To Suit 2

Reasons For Granting Certiorari 4

Argument

Point I

The Bankruptcy Court Is Not An Article III Court And, Absent Vigilant Supervision, Judicial Control and Actual Judicial Review It Is Not An Adjunct To The District Court. Petitioners Did Not Consent To The Invocation Of The Court's Jurisdiction By Its Order Directing An Adversary Proceeding By Filed 6

Point II

It Was Error For The Circuit Court To Endorse The Bankruptcy Court Order That Petitioners File An Adversary Proceeding. Thus Depriving Petitioners Of The Right To Trial By Jury Was Unconstitutional 13

Point III

Seating A Retired Annuitant Exceeded The Powers Of The District Court 18
A. The Federal Rules Of Civil Procedure Do Not Empower The District Court To Appoint Retired Annuitants As Bankruptcy Judges, Even In "Exceptional Circumstances" 18

B. The Transition Statutes AndThe Emergency Rule Do Not Empower The District Court To Appoint Retired Referees As Bankruptcy Judges, Even In "Exceptional Circumstances" 23

Summary Of Argument 28
Conclusion 29

Appendix A, Opinion of the Ninth Circuit A1
Appendix B, Order of Judge Seymour, Dated March 18, 1983 ..... B1
Appendix C, Excerpt from Plaintiffs' (Petitioners' Trial Brief) C1

TABLE OF AUTHORITIES CITED

Cases Page

Barton v. Barbour, 104 U.S. 126, 26 L.Ed. 672 (1881) 9
In Re Burley, 738 F.2d 981 (1984) 13, 14
Campbell v. United States District Court, 501 F.2nd 196, *cert denied,* 419 U.S. 879 (1974) 7
Carter, Danning, Joseph, etc. v. Lummis, etc., 12 B.C.D. 536 (C.D. Calif., 1984) 14, 18, 19, 22
Katchen v. Landy, 382 U.S. 323 (1966) 8
Myers v. United States, 272 U.S. 52 (1926) 28
In Re Morrisey, 717 F.2d 100 (3rd Cir. 1981) 14
Northern Pipeline Construction Co. v. Marathon Pipeline Co., 458 U.S. 50, 102 S.Ct. 2858 (1982) 5, 6, 12, 13, 19, 20, 21, 22, 24, 25, 26
Pacemaker Diagnostic Clinic of America, Inc. v. Instromedix, Inc., 712 F.2d 1305 (9th Cir. 1983) 6-7, 10, 11, 12, 22
Pacemaker Diagnostic Clinic of America, Inc. v. Instromedix, Inc., *En Banc*, 725 F.2d 537 (1984) 6, 12, 18
Ross v. Bernhard, 396 U.S. 531, 90 S.Ct. 733, 24 L.Ed.2d 729 (1970) 8, 9
United States v. Raddatz, 447 U.S. 667, 100 S.Ct. 2411 (1980) 14, 15, 20
1616 Reminic Ltd. Partnership v. Atchison & Keller, 704 F.2d 1313 (4th Cir. 1983) 14

Constitution

United States Constitution, Article 2, Section 2, Clause 2 28

Statutes

United States Code, Title 11
§241(a) 24
§404(D) 25

United States Code, Title 28
§152 ..... 23, 26, 27, 28
§153(a) 23, 26
§153(b) 23
§154 23
§404(b) 23, 27
§404(d) 25, 27
§451 24
§452 23
§636(c) 6
§636(c)(1) 6
§636(c)(2) 6
§1471 ..... 24, 25
§1471(a) 24
§1471(b) 24
§1471(c) 13, 24
§2072 ..... 19, 21
§2075 ..... 19, 21
Bankruptcy Amendments and Federal Judgeship Act of 1984 ..... 21, 27

Rules

The Emergency Rule—The Model Rule; Entered by Order of the District Court, Central District of California, December 27, 1982 ..... 10, 14, 16, 17, 18, 19, 21, 22, 23, 24, 25, 26, 29
Federal Rules of Civil Procedure, Rule 53 24

Other Authorities

5 Moore's Federal Practice ¶ 38.11[2] (2d ed. 1980) 9

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PETITION FOR WRIT OF CERTIORARI

STATEMENT

This matter was tried in the United States Bankruptcy Court for the Central District of California. It was tried to the Court without a jury. The Honorable Russell Seymour presided. All defendants were represented throughout the trial by counsel for Tokai Bank.

The Bankruptcy Court made findings of fact, conclusions of law, and a proposed judgment, and

referred the matter to the District Court on September 15, 1983. On September 16, 1983 the District Court, (Judge Manuel Real), entered a judgment dismissing the action.

Petitioners appealed. The Ninth Circuit in its memorandum decision filed December 17, 1985, affirmed.[1]

A. Preliminary

Petitioners had filed a voluntary Chapter 11 reorganization on January 20, 1981. Tokai Bank was a secured creditor. Gill was appointed Trustee and the proceeding was converted to a Chapter 7 liquidation.

An adversary proceeding in the Bankruptcy Court was filed on March 23, 1983. The Bankruptcy Court had earlier found "that the relief being sought in the Debtor's Application should be requested in the context of an adversary proceeding to be governed by the rules applicable to adversary proceeding." The Court ordered "the pending application is hereby dismissed . . . and if the debtors intend to proceed . . . they *shall* proceed by filing a proceeding under the Adversary Rules on or before March 23, 1983 . . . in accordance with Bankruptcy rule 704." (emphasis added)[2]

B. Factual Summary. The Circumstances Prior To Suit.

The property of the Estate was auctioned on December 12, 1982 after the Bankruptcy Court entered its order dated November 24, 1982.[3] Prior to the November 24,

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[1]Appendix A, this Petition.

[2]Order dated March 18, 1983, Appendix B, this Petition.

[3]The property (assets) consisted of a residential estate in Malibu on 8 acres, owned by Lawrence J. Galardi, MAI appraised at $3.5 million (hereinafter, "Eagle Pass"); and, 29 acres overlooking the

1982 Order, an adversary proceeding initiated by the defendant Trustee seeking leave to sell free and clear was restored to the calendar. It was heard on November 9, 1982 and summarily resulted in an Order dated December 7, 1982, authorizing sale free and clear. That Order relied upon a stipulation of Tokai and the Trustee permitting Tokai to submit its beneficiary demand in full, and requiring immediate payment.[4] The Court also relied upon the stipulation of the Trustee and Cambridge, another secured creditor, for the full amount of its claim. That Stipulation was so ordered on November 12, 1982.

A confidential letter agreement dated October 8, 1982 between Tokai Bank and the defendant Trustee, set forth their agreement to make joint application to employ an auctioneer; establish a minimum credit bid for the 29 acres; establish financing terms for the 29 acres; allow the fully secured claim of Tokai; and, establish a formula for credits based on a financed sale of the 29 acres. That Application was heard and fully allowed over objections for lack of notice to debtors and to general creditors, as to the confidential agreement.[5] The Court ordered the 29 acres be sold prior to the Eagle Pass property. However, the 29 acres was secondary security, only.

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ocean in Malibu, owned by Lawrence J. Galardi and Shari J. Galardi, MAI appraised at over $2.7 million, (hereinafter, "the 29 acres"). Liabilities in the reorganization were approximately $1.9 million.

[4]During the trial Petitioners sought to, among other matters, compel disclosure by Tokai of interest it claimed. The Court ordered disclosure and later reversed itself and agreed with counsel for the Bank that disclosure was not required.

[5]The Confidential Letter Agreement was not disclosed until the hearing on November 15, and only after the Court ordered it be disclosed.

The auction was conducted on December 12, 1982. A transcript of the auction proceeding was introduced at trial. At the auction, there was confusion. The auctioneer refused to respond to questions; there was confusion as to the terms of the prospective sales because of inconsistencies between the advertising and the auctioneers and the Trustee's representations. Bidding was chilled and prevented.

After the December 12, 1982 auction, the Trustee transferred title to the 29 acres to Tokai Bank and thereafter, Tokai by Grant Deed transferred title to a "customer of the Bank". The estate received a credit of only $641,000, as a result of Tokai's taking the property.

Reasons For Granting Certiorari

ARGUMENT

1. Petitioners respectfully submit the decision below must be reversed because:

A. Petitioners were deprived of their constitutional right to adjudication by an Article III Court;

B. The Bankruptcy Court was improperly constituted; and,

C. The Bankruptcy Court denied Petitioners the right to a jury trial ordering the Petitioners to file an adversary proceeding.

2. The Bankruptcy Court relied upon the Emergency Rule when the Court ordered Petitioners file an adversary proceeding, when it made its referral to the District Court and when the judgment appealed from below was signed by Judge Real without review as required by the Rule.

3. The Emergency Rule provided a mechanism for avoiding exercise of Article III powers by judicial bodies without tenure, but, that feature of its constitutionality had nothing to do with the power of the District Court to either seat a Bankruptcy Judge outside the provisions of the transition statutes; rubber-stamp a non-core matter as the District Court did here; or, lend the weight and authority of its judicial power to the unconstitutional exercise in the Bankruptcy Court that resulted in depriving Petitioners of a trial by jury.

4. While the Emergency Rule may have been a constitutional exercise within the context of the need to maintain a functioning bankruptcy system after *Marathon*,[6] the conduct of the Bankruptcy Court in this proceeding occasioned error, as a matter of law. Likewise, the conduct of the District Court, in failing to conduct a review. The conduct of both courts deprived Petitioners of their basic constitutional rights to a jury trial by an Article III Court. That excess was compounded when the District Court merely endorsed the result reached after ten full trial days, signing the judgment appealed from the day after it was submitted for a mandatory full and complete review under the Emergency Rule.

Accordingly, the judgment should have been reversed by the Ninth Circuit, and the matter remanded for trial on the issue of damages, only.

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[6]The Ninth Circuit erroneously stated and decided a *non-issue*, namely the constitutionality of the bankruptcy court after *Marathon*.

POINT I

THE BANKRUPTCY COURT IS NOT AN ARTICLE III COURT AND, ABSENT VIGILANT SUPERVISION JUDICIAL CONTROL AND ACTUAL JUDICIAL REVIEW IT IS NOT AN ADJUNCT TO THE DISTRICT COURT. PETITIONERS DID NOT CONSENT TO THE INVOCATION OF THE COURT'S JURISDICTION BY ITS ORDER DIRECTING AN ADVERSARY PROCEEDING BE FILED.

In *Pacemaker v. Instromedix etc.*, 725 F.2d 537 (1984), The Magistrates' Act and specifically 28 U.S.C. §636(c), was exhaustively examined against the background of special designation by the United States District Court (28 U.S.C. §636(c)(1)) and procedures established to prevent Magistrates from coercing litigant consent (28 U.S.C. §636(c)(2)).

The Supreme Court's decision in *Marathon* was earlier addressed by the Ninth Circuit Panel in August 1983, as follows:

> "A plurality of the Supreme Court plus two concurring justices held the Bankruptcy Court system to be unconstitutional. The plurality reasoned that bankruptcy judges were not Article III Judges, that the Bankruptcy Courts were not constituted as Article I Courts, and that the Bankruptcy Courts could not properly be considered "adjuncts" to the District Court. The plurality also held that the invalidity of the Bankruptcy Courts would only be applied prospectively."[7] *Pacemaker Diagnostice Clinic*

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[7]Prospective relief would be entirely appropriate here, as hereinafter appears.

of America, Inc., v. Instromedix, Inc., 712 F.2d 1305 (9th Cir. 1983), at P. 1308.

In the within action while the Bankruptcy Court referred its decision to the District Court for review pursuant to ¶(d)(3)(A) and (B), no review of the contested issues was made and in view of the language of the judgment none was contemplated.

The Ninth Circuit cites *Campbell v. United States District Court*, 501 F.2d 196, 206, *cert. denied*, 419 U.S. 879 (1974) in holding that objections to the findings and conclusions of the bankruptcy court were a prerequisite to review by the district judge. *Campbell, supra,* in fact held Local Rule 505 (4) provides for a "review of a magistrate's decision by the Judge" upon a notice to the magistrate and the adverse party. In the case at hand *review is mandated.* No notice is required to afford entitlement to review and no objections are required. *Campbell, supra,* is thus not only distinguishable, it is, Petitioners respectfully submit, utterly without applicability, here. In any case, the Referral stated the objections of Petitioners.

At the outset, there were issues of Article III power, Article I power, adjunct courts, Special Master powers and Reference powers, to be decided. In its Referral the Bankruptcy Court stated the adversary proceeding was a "core proceeding". No mention of any review by the District Court of any jurisdictional issues is made in the judgment of the District Court. The District Court stated the "United States Bankruptcy Court having heard and reviewed the evidence adduced at trial . . . the court having reviewed the matter together with the bankruptcy judges report and recommendations, and the Findings of Fact and Conclusions of Law having been duly signed, . . .", and endorsed the decision of Judge Seymour.

The District Court did not address itself to the requirement of litigant consent. The Bankruptcy Court had ordered Petitioners to file an adversary proceeding thereby denying the jury trial. The District Court totally ignored that, however, in adopting the Conclusions of Law and reached totally unsupported conclusions, holding; "*at no time* did the Bankruptcy Court order the plaintiff's to file an adversary proceeding in the Bankruptcy Court challenging the validity of the auction sale . . ." (emphasis added); but see, the order of Judge Seymour who in fact ordered "they (Petitioners) *shall* proceed by filing a proceeding under the adversary rules . . ."; and found further that "plaintiffs . . . have submitted to the jurisdiction of the Bankruptcy Court by filing their complaint . . ."; (Appendix B, this Petition) and Plaintiffs "have waived any right they may have had to object to the Bankruptcy Court's jurisdiction to hear this case."

The Ninth Circuit affirmed, erroneously relying upon *Katchen v. Landy*, 382 U.S. 323, 336-40 (1966).

The Ninth Circuit said;

> "Because bankruptcy proceedings are inherently proceedings in equity, the constitutional right to a jury trial, does not apply." (Appendix B, this Petition.)

While that decision is "not for publication," the Supreme Court, Petitioners submit, must grant certiorari here in order to right that unconstitutional exercise. *Ross v. Bernhard*, 396 U.S. 531,438 n.10, 90 S.Ct. 733, 24 L.Ed.2d 799 (1970).

The Seventh Amendment, Petitioners submit, preserves the right to jury trial in actions at law as it existed under the common law. It thus has no application to suits in equity or admiralty or to administrative

proceedings. *See* 5 *Moore's Federal Practice* ¶38.11[2] (2d ed. 1980). Hence, the primary determination which must be made is whether the cause of action sounds in law or equity. That bankruptcy courts act as courts of equity, *see, e.g., Barton v. Barbour,* 104 U.S. 126, 26 L.Ed. 672 (1881), is not dispositive of the matter, however, for the right to jury trial "depends on the nature of the issue to be tried rather than the character of the overall action." *Ross v. Bernhard, supra,* at 538. The Supreme Court has set forth three factors which may properly be considered in determining whether a particular claim or issue is legal or equitable: "first, the premerger custom with reference to such questions; second, the remedy sought; and third, the practical abilities and limitations of juries." Id. at n.10.

The District Court adopted the conclusion that "plaintiffs waived any rights they may have had to a jury trial." That was error, as a matter of law. It is clearly erroneous and is not supported in the record, as a matter of fact. The Circuit Court failed to differentiate the Article III rights involved here and the erroneous and baseless conclusion below that this was a "core proceeding," as hereinafter appears.

Judge Seymour's order dated March 18, 1983 states:

> " . . . Ordered that if the debtor's intend to proceed with the relief sought in their application they shall proceed by filing a proceeding under the adversary rules on or before March 23, 1983 . . . " (Appendix B, this Petition)

The plain and simple language mandated an adversary proceeding. The District Court took no note of that, or the record of objections to this proceeding on March 2, 1983, and at the trial, or, *the contradictory language of the Referral.*

The Emergency Rule (General Order 242-A) adopted in the District Court on December 27, 1982 provides at §(d) thereof:

"Powers of Bankruptcy Judges

(1) The bankruptcy judges may not conduct:

(D) Jury Trials"

The Bankruptcy Court made no pre-trial finding that the matters litigated in this adversary proceeding constituted a "core proceeding". After the trial, that was adopted by the District Court, in its judgment, but the basis for that conclusion is nowhere stated in the Findings of Fact and Conclusions of Law.

The only explanation for the error of both fact and law plainly apparent on this issue lies in the fact that the document was drawn by counsel for Tokai Bank and it was simply endorsed and rubber-stamped by Judge Seymour and by the District Court.

The plain language of the Order dated March 18, 1983 makes it clear that neither Judge Seymour nor Judge Real would have or could have thus agreed with counsel for Tokai unless they failed to consider that Order. Petitioners respectfully submit, neither could have ignored the literal meaning of the March 18 Order had they simply read it. There is no basis therefore for the Ninth Circuit thus ignoring Petitioners' Seventh Amendment rights.

Further, with regard to litigant consent and the exercise of judicial power, the Ninth Circuit, had by that time in September 1983, reviewed the power of those judicial bodies that give the appearance of functioning as an adjunct to an Article III Court. In *Pacemaker, supra,* the analogous position of litigants before special masters was focused upon, as follows:

> "No case squarely holds that litigant consent will solve the constitutional problems. In *Kimberly v. Arms*, 129 U.S. 512 (1889), the Supreme Court held that upon the consent of the parties a master could hear the matter and report findings of fact and law to the judge. Responsibility for the ultimate decision remained with the judge, and so "judicial" power was not vested in the master. To the same effect are the Coolidge (637 F.2d 132) and Raddatz (447 U.S. 667) cases, . . .[8] *Pacemaker, supra,* at p. 1311.

The Ninth Circuit had further addressed litigants' due process rights and their rights to judicial resolution by Article III Judges, in 1983, saying:

> "The use of Magistrates to conduct trials and enter final judgment implicates both due process and Article III concerns. We recognize that a due process right may be waived voluntarily, but there is more at stake here than the litigants due process right to a decision by an Article III Judge. We believe that the constitution establishes a framework of government that cannot be altered by statute nor waived by litigant consent. The independence of the judiciary, the distribution of power, and the separation of powers are at issue here.
> . . .

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[8]Please see Point III, this Petition, for a discussion of Judge Seymour's status on June 21, 1983 as a retired annuitant appointed as a Bankruptcy Judge by the District Court and after this trial, appointed as a Special Master, only, upon the withdrawal of his status as a "Bankruptcy Judge," by the District Court *because he was a retired annuitant.*

> The basis of the consent argument is that the right to an article III judge is a due process right, inuring to the benefit of litigants, and therefore waiveable like any other due process right. See footnote 10, *supra. Glidden Co. v. Zdanok*, 370 U.S. 530 (1962), refutes this contention . . . the Court indicated that *Article I Judges may not bind litigants in Article III Courts*, no matter how fairly they run the proceedings. The plurality specifically praised the qualifications, fairness, and impartiality of the judges involved. 370 U.S. at 533 (plurality opinion). Due process had been satisfied by the lower courts proceedings. If the right to an Article III Judge was only a due process right, the plurality would have terminated its discussion by noting the fair proceedings. See 370 U.S. at 533." *Pacemaker, supra,* at p. 1312. (emphasis added)

The Panel's analysis of the litigant's right to Article III adjudication was undisturbed by the Court *En Banc* and both the plurality and concurring opinions in *Northern Pipeline Construction Co. v. Marathon Pipeline Co.*, 458 U.S. 50, 102 S.Ct. 2858 (1982) were relied upon, in that regard. (*Pacemaker, supra,* 725 F.2d 537, (1984).)

There is nothing in the case at hand that warrants or justifies other than even-handed treatment here. Petitioners are at a loss to explain why the unpublishable opinion below is so violative of the earlier recognition of constitutional guarantees bestowed in *Pacemaker, supra.*

Petitioners complained of their being deprived of their constitutional right to a trial by jury through the

decidedly unfair mechanism of ordering an adversary proceeding. They complained that the renovation of the Bankruptcy Court system, if it can be called that, pending curative legislation, denied access to Article III judicial powers because of the initiating order (March 18, 1983) of Judge Seymour.

This denial of Article III adjudication was reason for reversal, below, as a matter of law and Petitioners submit it is reason for granting certiorari.

POINT II

IT WAS ERROR FOR THE CIRCUIT TO ENDORSE THE BANKRUPTCY COURT ORDER THAT PETITIONERS FILE AN ADVERSARY PROCEEDING. THUS DEPRIVING PETITIONERS OF THE RIGHT TO TRIAL BY JURY WAS UNCONSTITUTIONAL.

In each of the post *Marathon* decisions reviewing both trial proceedings, the Emergency Rule, and those decisions upholding the jurisdiction of the Bankruptcy Appellant Panels, (before the stay in *Marathon* expired), it is clear the circuits uniformly agreed *Marathon* struck down the trial court jurisdiction of Bankruptcy Judges as conferred by 28 U.S.C. §1471(c). Those decisions uniformly found that where the District Court conducted a review and retained the essential attributes of judicial power, constitutionality was assured, and where the District Court *did not* conduct an actual review the essential attributes of judicial power were not retained, the exercise was unconstitutional for the reasons set forth in *Marathon*. *In re Burley*, 738 F.2d 981 at page 985 (1984).

> Significantly, *Burley* relied on the fact that "parties not in Bankruptcy Appellate Panel

districts receive review in the first instance by an Article III Judge, while those in Bankruptcy Appellate Panel districts do not." *Burley, supra,* at page 98.

It is clear therefore, that a rubber-stamp endorsement is not a review at all.[9]

The entry of the final judgment by Judge Real, without review, was an unconstitutional exercise as the Emergency Rule mandataed there be review of the proceedings of the Bankruptcy Court.

Assuming *arguendo,* there was power to preclude a jury trial and hear the issues to the court alone, the failure to conduct a review in the District Court constituted a failure to abide the attempted jurisdictional cure afforded by the Emergency Rule pending remedial legislation.

The Ninth Circuit decision does not address that, the citation to *Campbell, supra,* to the contrary notwithstanding. And, certiorari, Petitioners respectfully submit, should be granted here since the rule of *U.S. v. Raddatz*, 447 U.S. 667, 680, 683 (1980) was misunderstood below.

Raddatz, supra, requires an actual review not simply the affixing of a signature so as to give the appearance that "the district judge acted as the ultimate decision maker." Appendix A, this Petition.

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[9]Reading the Findings and Conclusions, only, does not constitute a review. *Carter, Danning, Joseph, etc. v. Lummis etc., et al.*, 12 B.C.D. 536 (C.D. Calif., 1984). If this was a "core" matter, a clearly erroneous standard "has been held fully consistent with Article III principles." *Carter, supra,* citing *In re Morrisey*, 717 F.2d 100, at p. 104 (3rd Cir. 1981); *1616 Reminic Ltd. Partnership v. Atchison & Keller*, 704 F.2d 1313 (4th Cir. 1983).

The decision of the Circuit Court *ignores* this Court's requirement as spelled out in *Raddatz*.

Whether this is a "core"matter or a "related proceeding" is of no moment, in so far as conducting a review is concerned, in view of the language of the Referral. Clearly, constitutionality turns upon the requirement that the District Court

> "subject the Magistrate's—(here, Judge Seymour's)—proposed findings and recommendations to *de novo* review before entering a final order. It was on the basis of this requirement that the Supreme Court found the authority and the responsibility to make an informed, final determination . . . remains with the judge", *United States v. Raddatz*, 447 U.S. 667, at 682, 100 S.Ct. at 2415 (1980).

On that basis, the Supreme Court found the Magistrates Act met Article III standards in *Raddatz*. The Ninth Circuit opinion cites *Raddatz*, here, but ignores its critical feature, i.e., that the Article III Court *conduct a de novo* review.

Once again, if the analogy to the Magistrates Act is to be upheld and the constitutional test thus applied is to pass scrutiny here, it is necessary that the District Court have made an informed, reasoned, final determination based upon the record before signing the judgment on September 16, 1983, the day following its submission by Judge Seymour. To thus reasonably conclude on the state of this record, and taking into consideration the volume of the Trial Court record, is, Petitioners submit, impossible. Furthermore, all of the exhibits were "lost" by the Bankruptcy Court at some time prior to the appeal, and, after Judge Real's endorsement of the Seymour action, stipulated copies

of the trial record had to be made available for the Circuit Court. The District Court may not or, more likely, probably did not have the record before it during the 24 hours or less prior to signing the judgment. The stipulation is a part of the Ninth Circuit record on appeal.

The Report, Recommendation and Certification for Review indicates the referral to the United States District Court is in accordance with Emergency Rule §(d)(3)(A) and (B).

The Report and Recommendation further asserts the adversary proceeding "is a core proceeding under §(d)(2) of the Emergency Rule", and most importantly states, but *because of the jurisdictional objections* "the circumstances relating to this adversary proceeding require that the judgment *should be entered* by a United States District Court judge." (emphasis added.)

Clearly, no further objections were necessary as suggested by the Ninth Circuit and hereinabove treated in the discussion of *Campbell, supra.*

Judge Real entered the judgment. He did not conduct a review. He was aware, if he read the Referral, before he signed the judgment, that there were substantial objections.

The foregoing provisions of §(d)(3)(A) and (B) are those that clearly mandate an Article III Court conduct a review of related proceedings.

The Emergency Rule states:

> "§(2)(A) a District Court *shall* review: . . . (III) a proposed order or judgment lodged under §(d)(3), whether or not any notice of appeal or application for leave to appeal has been filed." (emphasis added).

Presumably, the absence of a specific requirement that objections be filed does not vitiate the requirement that

the District Court conduct a *de novo* review, especially since no notice of appeal is required. The opinion below implies a contrary rule and Petitioners submit that is reason for granting certiorari, here where there are especially clear and repeated indications of objections and disputed legal conclusions and factual findings cited in the Referral.

Thereafter, the Rule grants discretion to the District Judge as to *method* and states:

> "(B) In *conducting review* the District Judge may hold a hearing and may receive such evidence as appropriate and may accept, reject or modify, in whole or in part, the order or judgment of the Bankruptcy Judge, and need give no deference to the findings of the Bankruptcy Judge. *At the conclusion of the review*, the District Judge *shall* enter an appropriate order for judgment." (emphasis added).

While there is discretion then as to the means of conducting the review, there is no discretion as to whether a review shall be conducted.

Here, there was no review conducted of the record between the submission of the proposed findings and conclusions on September 15 and the signing of the judgment on September 16, 1983.

If this matter, *arguendo*, was a "related proceeding" as suggested (and notably disputed) in the submission prepared by Tokai Bank for the Bankruptcy Judge, a *de novo* review was mandated in order to assure the constitutional exercise of power by an Article III Court—the District Court—and not the Bankruptcy Court. The perfunctory signing of the judgment did not constitute a *de novo* review sufficient to assure the exercise of

that power so jealously retained by the District Court for purposes of assuring the constitutionality of decisions reached in the Bankruptcy Court in "related proceedings".[10]

The District Court had been fully apprised here of the jurisdictional dispute. Nevertheless, the District Court failed to review that dispute. The Ninth Circuit has chosen to ignore that omission. The Findings, Conclusions and Judgment, therefore, *were not* the result of adjudication by an Article III Court. This cannot be construed to be "active supervision of (an) Article III Judge(s)", or the "Continued and vigilant supervision by (an) Article III Judge(s) . . . essential to the integrity of the system . . . " *Pacemaker, supra*, 725 F.2d 537, at p. 546. Accordingly, for this reason too, certiorari should be granted.

POINT III

SEATING A RETIRED ANNUITANT EXCEEDED THE POWERS OF THE DISTRICT COURT.

A. The Federal Rules Of Civil Procedure Do Not Empower The District Court To Appoint Retired Annuitants As Bankruptcy Judges Even In "Exceptional Circumstances".

Petitioners respectfully submit the Federal Rules are not constitutionally available to implement a system of bankruptcy courts and judges anymore than the Congress can confer Article III powers through the Magistrates Act.

The Congress has said the Federal Rules, prescribed by the Supreme Court, shall not "abridge, enlarge or

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[10]*Carter, supra; Pacemaker, supra*, 725 F.2d 537 (9th Cir. 1984); and, the Emergency Rule, *supra*.

modify any substantive right". (28 U.S.C. §2072). The Supreme Court was empowered to prescribe rules for the practice and procedure to be followed under Title 11, the Bankruptcy Act of 1978. Those rules too, "shall not abridge, enlarge, or modify any substantive rights". (28 U.S.C. §2075).

The Emergency Rule adopted by the Executive Committee of the Judicial Conference and implemented by order of the United States District Court (entered December 27, 1982), cannot serve to expand, limit or modify rights that have constitutional protection. Judicial supplementing of existing law, Petitioners submit, is appropriate only where it does not transgress upon the power of the Congress. Only the Congress has the power to enact appropriate remedial legislation, curing the unconstitutionality of the earlier grant of power to Bankruptcy Judges. Clearly, were it possible to cure the lack of subject matter jurisdiction by rule-making, there would have been absolutely no reason for this Court to stay its judgment in *Marathon*.

Although the Emergency Rule was arguably advanced as a "housekeeping" attempt pending remedial legislation, if it is not confined and scrupulously adhered to it in fact so substantially affects the rights of all persons (debtors and creditors alike) that it is equivalent to new legislation. That conclusion is inescapable in circumstances like those at hand where the resulting judicial body (retired Judge Seymour) takes it upon itself to exercise Article III powers over substantive rights. Pure and simple, that is the effect of Judge Seymour's order (March 18, 1983) entered at the urging of counsel for defendant Tokai;[11] and, the effect of the failure to review.

[11]The failure of Judge Real to conduct a review requires that conclusion, and, it further distinguishes the line of cases discussed in *Carter, supra*, where the constitutionality of the rule was upheld.

While in a proper case it might be argued that the failure of the Congress to act created procedural uncertainty on the one hand and removed available substantive remedies on the other, that was not the basis upon which the Bankruptcy Court ordered Petitioners file an adversary proceeding, without a jury. Tokai, cannot therefore be heard in these circumstances, to argue the need to cure procedural uncertainties and maintain and continue the bankruptcy court system.

That also appears to be the thrust of the Ninth Circuit language where it characterizes the issue on appeal as the constitutionality of *Marathon*. That simply is not the case.[12]

Tokai was successful in gaining the acquiescence of Judge Seymour in a conclusion of law that this was a "core proceeding". *That was purely an afterthought, and nothing more.* A cursory review of the Complaint by the District Court would have confirmed this was not a "core proceeding". It was a clear attempt at justification of the over-zealous pursuit below of a solution that would at once bestow credibility upon erroneous findings and conclusions of the Bankruptcy Court and justify having denied access to the judicial power of the United States, in an Article III Judge.

Prior to the Defendant inspired compulsion that an adversary proceeding was required under the bankruptcy rules without a jury, Petitioners argued there was sound

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[12]The within appeal involves the need for an adequate and demonstrable effort at review by the District Court. While the Supreme Court concluded in *Raddatz*, that taking testimony was not required in all cases it nevertheless maintained the rule that "review" meant conducting a review in order to reach an independent determination of the issues that required Article III adjudication. Judge Real did not do that and the Ninth Circuit opinion ignores that.

reason for the Bankruptcy Court to decide an Article III Court should hear the matter. The authorizing statute pursuant to which the Judicial Conference presumably acted mandating substantive rights not be "abridged, enlarged or modified" in enacting 28 U.S.C. §§2072 and 2075 was placed within Judge Seymour's focus and Petitioners argued the result reached in *Marathon, supra,* be regarded as a mandate requiring all substantive matters involving state created rights, or substantive rights that were provided by the Congress, be stayed pending the enactment of legislation, or an Article III Court was required. The specialized expertise necessary to the determination of bankruptcy matters—so-called "core proceedings"—could function in that environment without risk of violating the constitutional guarantees provided by Article III. Judge Seymour summarily rejected any consideration of those issues. Thereafter, Judge Real compounded the error with his utter disregard of the Rule.

Clearly, Judge Real regarded the Emergency Rule as an inspired attempt to continue the Bankruptcy Court system and he did so, as an Article I adjunct to the District Court in all matters regardless of whether the issues were purely core matters or matters of substantive rights requiring Article III adjudication. Counsel used the Referral procedure at will, recognizing (prior to 1984) that "review", as a practical matter, meant only "endorsement," at that time.[13] Clearly too, there was no consent and Petitioners' attempts to operate within the bankruptcy scheme evidence that, but, they also proved completely futile.

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[13]Prior to the enactment of the "Bankruptcy Amendments and Federal Judgeship Act" of 1984 P.L. 98-353, 98 stat. 333 (July 10, 1984).

Here, there were objections, there was no litigant consent and substantive rights were effectively foreclosed and without remedy. Thus abridging Petitioners' substantive rights, ordering an adversary proceeding, constituted an infringement upon Article III and fundamental rights to due process. It was in Tokai's interest to keep this matter in the Bankruptcy Court and not expose the continuing unconstitutional exercise and interference with Petitioners' substantive rights outside the Bankruptcy Court. There is no other reasonable explanation for the wording of the March 18, 1983, Court order.

Pacemaker, supra, denied bankruptcy judges any such aggrandisement of their power and re-affirmed *Marathon*.

Carter, supra, found the 1984 Act simply "codified" that Court's (Judge Takasugi) perception of review and the District Court's functioning under the Emergency Rule. The 1984 Act has been tested somewhat and it is surviving. The Circuit, Petitioners submit, should have viewed the way the system functioned in practice, however, as opposed to how it was designed to function in theory under the Emergency Rule on September 16, 1983 (the date of the Judgment appealed from.) *In this case, it was not in all respects constitutional because of how it failed to function.*

The courts below have denied Petitioners the exercise of their constitutional right to a jury trial. Their decisions have clearly "altered, abridged and modified" Petitioners' substantive rights to the real property, in these circumstances, in exercising Article III power. That is the effect of there having been no review here by the District Court as mandated by the Emergency Rule. Without review, the rubber-stamp procedure indulged

here makes the judgment appealed from a judgment of the Bankruptcy Court and not the District Court. For that reason, too, Petitioners submit, this Court should grant certiorari.

B. The Transition Statutes And The Emergency Rule Do Not Empower The District Court To Appoint Retired Referees As Bankruptcy Judges, Even In "Exceptional Circumstances".

The Emergency Rule provided for a general reference to the Bankruptcy Judges of the Central District ((C)(c)(1)) ("Reference to Bankruptcy Judges"). Those judges had been *appointed to office for 14 year terms by the President*, with the advice and consent of the Senate (28 U.S.C. §§152, 153(a)), and were subject to removal by the "Judicial Council of the Circuit" on account of incompetence, misconduct, neglect of duty or physical or mental disability" (28 U.S.C. §153(b)). In addition, the 1978 Act fixed their salaries making them subject to adjustment under the Federal Salary Act (28 U.S.C. §154).

Incumbent Bankruptcy Referees serving six year terms for compensation were designated to serve as Bankruptcy Judges until March 31, 1984 or until their successors took office (28 U.S.C. §404(b)). The District Court by Order dated November 12, 1982, appointed Judge Seymour, *a Retired Annuitant*, to serve as a Bankruptcy Judge.[14]

28 U.S.C. §452 entitled "Definitions", identifies those judges who are judges of the Courts of Appeals, District Courts, Court of International Trade "and any Court

[14]Judge Seymour was not an "Incumbent Bankruptcy Referee". And, there is no provision in the so-called transition statutes as set forth in the Act of 1978 at §404(b) (92 stat. 2683) for District Judges to appoint retired Referees to the bench.

created by act of Congress, the judges of which are entitled to hold office during good behavior." (28 U.S.C. §451). Judge Seymour had earlier retired from office as a Referee.

In the 1978 Act Congress intended original but not exclusive jurisdiction in the District Court in matters arising under Title II (28 U.S.C. §1471(b)). That jurisdiction was to be exercised by the newly created Bankruptcy Court and the judges of that Court serving without tenure. For those reasons, i.e., the unconstitutional exercise of Article III judicial power, the Supreme Court concluded in *Marathon, supra,* that 28 U.S.C. §1471 violated Article III. This Court further concluded that since Article III bars Congress from establishing under its Article I powers, legislative courts to exercise jurisdiction over all matters arising under the bankruptcy laws, the grant of jurisdiction could not be sustained as an exercise of Congress' power to create adjuncts to an Article III Court.[15] The Bankruptcy Court therefore functioned solely (at the time of the trial below) by virtue of the Emergency Rule.

It also must be concluded that the appointment by the District Court of a retired annuitant, a private citizen as it were, who did not have status as a judge of any

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[15] *Marathon* held §241(a) was non-severable and it struck the entire statute, leaving no remnant of power in either the Bankruptcy Court or the District Court. Petitioners respectfully submit without some remnant of power the District Court had no basis upon which to appoint the Retired Annuitant except as a Special Master under F.R.C.P. 53. Assuming *arguendo* that there is room to conclude §241(a) was severable, the mandatory reference called for in 28 U.S.C. §1471(c) is exclusive and prevents the exercise of power by the District Court under §§1471(a) and 1471(b). There is no room to conclude therefore, that the District Court had *any* authority in the case at hand to appoint a retired annuitant or refer cases to a retired annuitant who had no standing as a judge of a United States court.

court created by act of Congress, was improper. The District Court was neither empowered under the so-called transition statutes ((§404)(d)) or any other power including the power hereinabove discussed in the Emergency Rule to thus deal with the exceptional circumstances found to exist by virtue of the Supreme Court's decision in *Marathon.*

Uncomfortable as thus concluding may be, the fact remains there was no authority pursuant to which the District Court could designate Judge Seymour to sit.

If it is argued that thus striking the power of Judge Seymour to sit may cause hardship in cases earlier decided by the retired annuitant, Petitioners respectfully request this court deal with the matter *prospectively*, assigning the same rationale utilized by the Court in *Marathon, supra.*

Further, with regard to whether the Emergency Rule gave power to appoint a Judge, Petitioners respectfully request this Court consider its stay of judgment in *Marathon* and the reasons for that stay. Clearly, if the unconstitutionality of the jurisdictional grant in §1471 could be papered over by Rule of Court there would not have been a need for a stay. The stay was deemed necessary to "afford Congress an opportunity to reconstitute the Bankruptcy Courts or to adopt other valid means of adjudication without impairing the interim administration of the bankruptcy laws" *Marathon, supra.* Indeed, had it been possible for the Supreme Court with its rule making power to confer the power that was absent for want of jurisdiction, Petitioners respectfully submit, this Court need not have waited for the District Courts to enact an Emergency Rule. Absent, curative and remedial legislation then, the bankruptcy system was placed in a jurisdictional void on June 28, 1982 and that void was not filled by the

Emergency Rule of December 27, 1982, not sufficiently at least to justify *each* of the unconstitutional exercises hereinabove argued.

The bankruptcy system continued while Congress continued to consider remedial legislation. During the congressional exercise, disagreement over the status of Bankruptcy Judges and the nature of the power that was to be conferred upon them, increased. The House Judiciary Committee reported its conclusions, (significantly, in early 1983), that an Article III Bankruptcy Court was needed. (H.R. 3, 98th Congress, Rep. No. 9, Pt. 1, 1st sess. (1983)). Later the Senate Judiciary Committee reported a bill establishing non-Article III Bankruptcy Judgeships to "assist the District Courts" which would "retain" bankruptcy authority (S. 1013, 98 Congress; see S. Rep. No. 55, 98 Congress, 1st sess. (1983)). That report concluded as the Supreme Court had concluded in *Marathon* that the jurisdictional grant to the United States District Court was to be exercised exclusively by the Bankruptcy Court, which was a "non-adjunct" Court, a "non-legislative" Court and a "non-Article III" Court.

Neither report addressed the fact that the *1983* jurisdiction of the Bankruptcy Courts was derived from the Emergency Rule and the District Court did not have the power to legislate. Nor were the inconsistencies between the Emergency Rule and the Bankruptcy Rules (as promulgated by the Supreme Court on August 1, 1983) addressed.

Shortly prior to the termination of the transition period, the House agreed with the Senate position and Bankruptcy Judges[16] were made "adjuncts" of the District Court. (See, H.R. 5174, 98 Cong., 2nd Sess.

[16]Appointed in accordance with 28 U.S.C. §§152 and 153(a).

with S. 1013, 98 Cong., 2nd Sess.) Thereafter an interim measure amending the 1978 Act extended the transition period for appointed Judges to April 30, 1984 (B.L. No. 98-249, 98 stat. 116 (March 31, 1984)). Another extension of the transition period to May 25, 1984 (P.L. No. 98-271, 98 Stat. 163 (April 30, 1984)) and a series of additional extensions of the transition period were then enacted prior to the agreement by both houses to the conference report in June of 1984.

The "Bankruptcy Amendments and Federal Judgeship Act of 1984," was the result. (P.L. No. 98-353, 98 Stat. 333, July 10, 1984.)

The 1984 Act resolved the transitioning of Bankruptcy Judges. It must be noted that the terms of the *judges then sitting by appointment* (28 U.S.C. §152), continued by operation of the holdover provisions in §§404(b) and (d) of the Bankruptcy Act of 1978.

The *retired annuitant sitting below was appointed by District Court Order outside the operation of the transition provisions and without benefit of being a retained Bankruptcy Judge in office after the expiration of a stated term or until a successor took office.*

The District Court had no power to thus act. The Ninth Circuit opinion erroneously relies upon 404(d) of the 1978 Act and 40 (d)(2) of the Act of 1898.

The Retired Annuitant was not a "sitting judge" within the meaning of the transition statutes. His earlier right to hold over as a referee had long since expired. There was no authority to appoint judges conferred upon the District Court by the 1978 Act and that authority is not inherent in the District Courts of the United States, in any case. It can not be said the need to avoid disruption of the bankruptcy system served to confer the power to appoint Judges. That is why the transition statute

and the holdover provisions were *critical to who was permitted to sit* during the period June 28, 1982 through July 10, 1984.[17] The Ninth Circuit opinion ignores that.

Finally, his appointment was clearly in violation of the "Appointments Clause" (Article II, section 2, clause 2 of the Constitution). Being neither a then sitting Bankruptcy Judge appointed under 28 U.S.C. §152, or an incumbent Referee, there was no constitutional authority for his holding-over and there was no constitutional authority for his appointment.

SUMMARY OF ARGUMENT

Certiorari should be granted. The memorandum decision of the Ninth Circuit does not accord with the law.

The District Court exceeded its authority in appointing a retired annuitant as a Bankruptcy Judge. There was no authority for that appointment in either the transition statutes, the holdover provisions, the Federal Rules of Civil Procedure or, by virtue of any provision of the Constitution of the United States.

The Bankruptcy Court deprived Petitioners of their constitutional right to a jury trial when it ordered them to proceed in the Bankruptcy Court and file an adversary proceeding.

---

[17]Had Judge Seymour been other than a retired annuitant, arguably, Article II, section 2, clause 2 of the Constitution might have colored the authority of the District Court to extend a sitting Bankruptcy Judge by virtue of the constitutional grant to the Congress of authority to vest appointment to inferior offices, as applicable, in the court of law. *Myers v. United States*, 272 U.S. 52, 128 (1926). But, Article II, section 2, clause 2 and 28 U.S.C. §152 cannot be circumvented by a District Court appointment. The Ninth Circuit opinion ignores that.

Following the conclusion of the trial the Bankruptcy Court made Findings of Fact that were clearly erroneous in material particulars and Conclusions of Law that were in error, as a matter of law and referred them to the District Court.

The Referral was pursuant to the Emergency Rule.

Upon receipt of the referral, Judge Real failed to conduct a *de novo* review in accordance with the Emergency Rule and simply rubber-stamped the decision of Judge Seymour. The documents referred were signed by Judge Seymour on September 15, 1983 and Judge Real signed the judgment on September 16, 1983.

CONCLUSION

For the foregoing reasons Petitioners respectfully submit their petition for a Writ of Certiorari should be granted.

DATED: February 13, 1986

Respectfully submitted,

LAWRENCE J. GALARDI
Attorney for Petitioners

APPENDIX

APPENDIX A

FILED

Not For Publication

DEC 17 1985

CLERK, U.S. COURT OF APPEALS

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

In re: LAWRENCE J. GALARDI, dba LAWRENCE J. GALARDI, a professional corporation, and SHARI J. GALARDI, Debtors.	No. 83-6385 Bkcy. Adv. No. LA 83-4052 RS MEMORANDUM
LAWRENCE J. GALARDI and SHARI J. GALARDI, Plaintiffs-Appellants, -vs- TOKAI BANK OF CALIFORNIA, a California corporation; DAVID A. GILL, Trustee in Bankruptcy for GALARDI, Defendants-Appellees.	

Appeal from the United States District Court
for the Central District of California
Manuel L. Real, District Judge, Presiding
Argued and Submitted November 4, 1985
Los Angeles, California

Before: WALLACE, HUG, and HALL,
Circuit Judges.

Lawrence and Shari Galardi (the Galardis) brought an adversary action in the bankruptcy court in order to set aside the auction sale of property pursuant to their prior chapter 7 liquidation proceeding. The bankruptcy judge made findings of fact, conclusions of law, and a proposed judgment, and referred the matter to the district court. The district court entered a judgment dismissing the action, and the Galardis appealed. We have jurisdiction under 28 U.S.C. § 1291, and we affirm.

The Galardis' first four arguments involve questions of law, which we review de novo. *United States v. McConney*, 728 F.2d 1195, 1201 (9th Cir.) (en banc), *cert. denied*, 105 S. Ct. 101 (1984).

The Galardis argue first that the exercise of jurisdiction by the bankruptcy court was unconstitutional under *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (*Marathon*). We disagree. The bankruptcy court acted pursuant to General Order No. 242-A of the United States District Court for the Central District of California. General Order No. 242-A complies with the requirements of article III and the holding of *Marathon*. *See Lucas v. Thomas (In re Thomas)*, 765 F.2d 926, 928-30 (9th Cir. 1985).

The Galardis also argue that they were deprived of their constitutional right to a jury trial. This argument is equally without merit. Because bankruptcy proceedings are inherently proceedings in equity, the constitutional right to a jury trial does not apply. *Katchen v. Landy*, 382 U.S. 323, 336-40 (1966).

Next, the Galardis argue that the district court's adoption of the bankruptcy judge's proposed judgment

violated the requirements of article III and due process. The Galardis contend that the district judge was required to review the entire record before entering judgment. We reject this argument. Because the Galardis did not make any objections to the bankruptcy judge's findings of fact or conclusions of law, the district judge properly made his determination on the basis of these findings and conclusions. *See Campbell v. United States District Court,* 501 F.2d 196, 206 (9th Cir.), *cert. denied,* 419 U.S. 879 (1974). Because the district judge acted as the ultimate decisionmaker, there has been no violation of the requirements of article III or of due process. *United States v. Raddatz,* 447 U.S. 667, 680, 683 (1980).

The Galardis also argue that the district court improperly appointed a retired bankruptcy referee to serve as bankruptcy judge. This argument is unsound. The district court's appointment of the bankruptcy judge was authorized by section 404(d) of the Bankruptcy Reform Act of 1978, which expressly reserved the authority, under section 40d(2) of the Bankruptcy Act of 1898, to appoint a retired referee to perform bankruptcy duties.

The Galardis also challenge several of the bankruptcy judge's evidentiary rulings. We review these rulings for abuse of discretion. *M.A.P. Oil Co. v. Texaco Inc.,* 691 F.2d 1303, 1310 (9th Cir. 1982). We see no merit in any of the Galardis' evidentiary contentions.

AFFIRMED.

Note: This disposition is not appropriate for publication and may not be cited to or by the Courts of this Circuit except as provided by Ninth Circuit Rule 21.

APPENDIX B

...ENTERED

... 1983

...K, U.S. BANKRUPTCY COURT
... DISTRICT OF CALIF...

FILED

MAR 18 1983

CLERK, U.S. BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIF...

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MAR ... 1983

... U.S. BANKRUPTCY COURT
... DISTRICT OF CALIF...

UNITED STATES BANKRUPTCY COURT
CENTRAL DISTRICT OF CALIFORNIA

In re:)	
LAWRENCE J. GALARDI dba)	Bankruptcy No.
LAWRENCE J. GALARDI,)	LA 81-00606-RS
a Professional Corporation,)	ORDER DISMISSING
and SHARI J. GALARDI,)	APPLICATION
Debtors.)	

On March 2, 1983, the debtors' application for order: (A) declaring this Court does not have jurisdiction; (B) declaring the auction of December 12, 1982 was illegal and a nullity; (C) setting aside any grant deed resulting from the auction of December 12, 1982; (D) compelling a trustee to execute a grant deed as to the eight (8) acre parcel known as 20600 Eagle Pass to the successful

bidder came on regularly for hearing before Judge Russell B. Seymour, bankruptcy judge presiding. Lawrence J. Galardi appeared in propria personna and John A. Graham of Frandzel & Share, A Law Corporation, appeared on behalf of Tokai Bank of California.

Having considered the written application and papers in support thereof, the memorandum of points and authorities in opposition to the debtors' application, and after considering all arguments, the Court finds that the relief being sought in the debtors' application should be requested in the context of an adversary proceeding to be governed by the rules applicable to adversary proceedings. Therefore, based on the foregoing findings, and good cause appearing therefore, it is

ORDERED that the pending application is hereby dismissed and it is further

ORDERED that if the debtors intend to proceed with the relief sought in their application they shall proceed by filing a proceeding under the adversary rules on or before March 23, 1983; and it is further

ORDERED that upon the commencement of said adversary proceeding, a summons and notice of trial shall be issued and served in accordance with Bankruptcy Rule 704.

Dated: March 18, 1983.

Russell B. Seymour

RUSSELL B. SEYMOUR
Bankruptcy Judge

APPENDIX C

EXCERPT FROM PLAINTIFFS' TRIAL BRIEF RE: ISSUES FRAMED BY THE COMPLAINT

The first cause of action seeks declaratory relief, declaring the Court is without jurisdiction of the subject matter and notwithstanding the direction that the within adversary proceeding be filed by plaintiffs, if plaintiffs were to seek the relief herein prayed for. The first cause of action, in sum, prays for judgment declaring this Court is without Article III judicial power to rule on the matters here in issue and cannot otherwise legally exercise Article III powers.

The issues of this Court's jurisdiction and this Court's lack of Article III powers and lack of jurisdiction of the subject matter are hereby expressly reserved. The Court has in other proceedings declared it believes it can lawfully exercise the powers in question and although plaintiffs do not accede, thereto, they recognize they are required to go forward here and do so on the basis of the aforesaid reservation of rights with regard to the jurisdictional issues.

The second cause of action seeks declaratory relief, declaring the auction of December 12, 1982 was illegal and was nullity:

(a) for failure to comply with the Court Order dated November 24, 1982;

(b) for failure to advertise properly;

(c) for misleading and misrepresenting material and substantial facts, prior to and at the time of the auction on December 12, 1982;

(d) for failing to conduct the action in accordance with reasonable auction practices;

(e) for fraud and unfairness resulting in depriving the bidding public, the debtors and the estate of

debtors of their rights to a fair and legal auction and judicial sale;

(f) for failing to provide for the full fair and free exchange of information prior to and at the time of the auction and thereby creating and fostering confusion, ambiguities, false information and otherwise interferring with a public auction in accordance with law;

(g) for failing to lawfully conclude the bidding on the 29 acre parcel;

(h) for explicit misrepresentations with regard to the properties auctioned;

(i) for discouraging the bidding public from bidding, to the disadvantage to the estate, the creditors and debtors with the express purpose of serving the advantage of Defendant, TOKAI BANK, only;

(j) for the misfeasance and malfeasance of the representative of the attorney for the Trustee;

(k) for defense counsel interference with the conduct of the auction;

(l) for the erroneous statements of law made by the auctioneer;

(m) for making last minute changes in auction terms that were not earlier advertised or reasonably known to the bidding public; and

(n) for conducting an auction that was unfair and fraudulent and did not accord a fair public auction to the bidding public or to the complainants, to the prejudice of debtors estate and in flagrant disregard of this Court's Order and the rights, duties and obligations of counsel as officers of this Court.

The third cause of action seeks declaratory relief declaring defendants' action violated the Stay provided by the Congress in 11 U.S.C. §362, et seq.

The fourth cause of action seeks a temporary injunction restraining defendants from attempting to obtain possession of either or both properties or otherwise disposing of or seeking to liquidate said properties prior to determination of the rights of the parties here in issue. (83-4052; Docket Entry #24)

PROOF OF SERVICE BY MAIL

State of California

ss.

County of Los Angeles

I, the undersigned, say: I am and was at all times herein mentioned, a citizen of the United States and a resident of the County of Los Angeles, over the age of eighteen (18) years and not a party to the within action or proceeding; that my business address is 11333 Iowa Avenue, Los Angeles, California 90025; that on February 13, 1986, I served the within *Petition for Writ of Certiorari* in said action or proceeding by depositing true copies thereof, enclosed in a sealed envelope with postage thereon fully prepaid, in the United States mail at Los Angeles, California, addressed as follows:

Clerk, United States
Supreme Court
One First Street, N.W.
Washington, D.C. 20543
(Original and forty copies)

Frandzel & Share
8383 Wilshire Boulevard
Suite 400
Beverly Hills, California 90211

Robinson, Wolas & Diamant
1888 Century Park East
Suite 900
Los Angeles, California 90067

I declare under penalty of perjury that the foregoing is true and correct. Executed on February 13, 1986, at Los Angeles, California.

Joy Rivelli Miller
(Original signed)

Supreme Court, U.S.
FILED
MAR 14 1986
JOSEPH F. SPANIOL, JR.
CLERK

No. 85-1368

IN THE
SUPREME COURT
OF THE UNITED STATES
October Term, 1985

LAWRENCE J. GALARDI AND SHARI J. GALARDI,

Petitioners,

vs.

TOKAI BANK OF CALIFORNIA, a California Corporation, et al.,

Respondents.

ON WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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451P

QUESTIONS PRESENTED

1. Were Petitioners denied a right to a jury trial?

2. Did the District Court properly review the Bankruptcy Court's findings of fact and conclusions of law and enter judgment thereon?

3. Did Section 404(d) of the Bankruptcy Reform Act of 1978 continue the District Court's appointment powers, permitting the District Court to appoint a retired bankruptcy judge as a bankruptcy judge pursuant to Section 40(d) of the Bankruptcy Act?

4. Should the Supreme Court grant *certiorari* when no important question of federal law is presented and when the decision of the Ninth Circuit is firmly based on long-standing authority?

INTERESTED PARTIES

Respondents submit that in addition to those persons specified as interested parties in the Petition for Writ of Certiorari, the following persons may arguably have an interest in the outcome of the case before this Court:

(1) Donald L. Lewis, a subsequent owner of the real property located at 20731 Cool Oak Way, Malibu, California; and

(2) Eagle Pass Associates, a California Limited Partnership, a subsequent owner of the real property located at 20600 Eagle Pass Drive, Malibu, California.

Dated: March 10, 1986

FRANDZEL & SHARE
A Law Corporation
STANLEY W. W. KESSELMAN
JOHN A. GRAHAM

By: STANLEY W. W. KESSELMAN
Attorneys for Respondent
TOKAI BANK OF CALIFORNIA

TABLE OF CONTENTS

Page

QUESTIONS PRESENTED i

INTERESTED PARTIES ii

TABLE OF AUTHORITIES v

I. STATEMENT OF THE CASE 1

A. Petitioners' Challenge of the Auction and the District Court Judgment 2

B. Issues Presented to the Court of Appeals and Affirmance of the District Court Judgment 4

II. SUMMARY OF ARGUMENT IN OPPOSITION TO GRANT OF CERTIORARI 5

III. PETITIONERS WERE NOT DENIED THE RIGHT TO A JURY TRIAL 6

IV. THE DISTRICT COURT'S REVIEW WAS CONDUCTED IN ACCORDANCE WITH THE EMERGENCY RULE AND SATISFIED THE REQUIREMENTS OF DUE PROCESS OF LAW 8

A. The Emergency Rule and the District Court Reference of the Adversary Proceeding Were Constitutional 8

B. The District Court Properly Reviewed the Bankruptcy Court's Determination and Properly Entered Judgment in Favor of All Defendants 10

V. THE DISTRICT COURT HAD AUTHORITY TO APPOINT JUDGE SEYMOUR TO SIT AS A BANKRUPTCY JUDGE 13

VI. PETITIONERS HAVE RAISED NO CLAIMS TO JUSTIFY REVIEW ON CERTIORARI 15

VII. CONCLUSION 16

APPENDIX 1

APPENDIX 2

TABLE OF AUTHORITIES

Page

Cases

United States Supreme Court

Katchen v. Landy,
382 U.S. 323, 336-340 (1966) 5, 7

Mathews v. Eldridge,
424 U.S. 319, 335, S.Ct. 893, 47 11

Northern Pipeline Construction Company v. Marathon Pipeline Company,
458 U.S. 50, 102 S.Ct. 2858, 73 L.Ed.2d 598 (1982) 7, 8, 10

United States v. Raddatz,
447 U.S. 667, 100 S.Ct. 406, 65 L.Ed.2d 424 (1980) 10-11

United States Courts of Appeal

Camby v. Davis,
718 F.2d 198, 199 (4th Cir. 1983) 12-13

Coast Steel Corporation v. Tilghman Wheelabrator, Ltd.,
709 F.2d 190 (3d Cir. 1983) 9

In Re Braniff Airways, Inc.,
700 F.2d 214, (5th Cir. 1983), *cert denied* 461 U.S. 944 (1983) 9

In Re Hansen,
702 F.2d 1573, 1578 (2d Cir. 1983) 9

In Re Kaiser,
722 F.2d 1573, 1578 (2d Cir. 1983) 9

In Re Stewart,
741 F.2d 127, 129 (7th Cir. 1984) 9

In Re Thomas,
765 F.2d 926, 929 (9th Cir. 1985) 9

Nettles v. Wainwright,
677 F.2d 404 (5th Cir. 1982) 12

Oklahoma Health Services Federal Credit Union v. Webb,
726 F.2d 624 (10th Cir. 1984) 9

White Motor Corp. v. Citibank, N.A.,
704 F.2d 254 (6th Cir. 1983) 9

Statutes, Acts, and Rules

Bankruptcy Act of 1898
Section 1(10) 4, 6, 14
Section 40(d) 6, 14
Section 40(d)2 ..... 4, 6, 14

Bankruptcy Reform Act of 1978, P.L. 95-598
Section 404(a) 4, 14
Section 404(d) 4, 6, 14

Bankruptcy Rule 9015 ..... 3, 5

Emergency Rule, United States District Court for the Central District of California, Local Rule Governing Bankruptcy Cases and Proceedings, Effective December 25, 1982 ..... 4, 7-10
Rule (d)(3)(B) 10
Rule (e)(2)(B) 10

United States Code

28 U.S.C. § 1471(a) 9
28 U.S.C. § 1471(b) 9
28 U.S.C. § 2071 9

Treatises

Collier On Bankruptcy, 15th Edition, Volume I,
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No. 85-1368

IN THE
SUPREME COURT
OF THE UNITED STATES
October Term, 1985

LAWRENCE J. GALARDI AND SHARI J. GALARDI,

Petitioners,

vs.

TOKAI BANK OF CALIFORNIA, a California Corporation, et al.,

Respondents.

OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

I

STATEMENT OF THE CASE

This litigation arises out of an auction of two parcels of real property which had been part of the Petitioners' bankruptcy estate. The auction was conducted by the Chapter 7 bankruptcy trustee pursuant to an order of the Bankruptcy Court approving the sale. This Petition for Writ of Certiorari represents the final chapter in the saga of Petitioners' unrelenting efforts to thwart the trustee's

proper exercise of his statutory duty to liquidate the property of the debtors' Chapter 7 estate.

A. Petitioners' Challenge of the Auction and the District Court Judgment .

On November 24, 1982, the Bankruptcy Court entered an order directing the trustee to conduct an auction sale of two parcels of real property of the Galardi bankruptcy estate. The order approving the sale was granted upon the joint application of the Chapter 7 trustee, David A. Gill, and Tokai Bank of California, the holder of first deeds of trust on the two parcels of property.[1] The sale was conducted on December 12, 1982.

Thereafter, on January 20, 1983, Petitioners filed an *unverified* Application before the Bankruptcy Court requesting the Court to set aside the auction sale and to quiet title to the real property in Petitioners' name. In light of Petitioners' challenge to the trustee's conduct of the sale under the Court's order, and the need for substantial documentary and testimonial evidence to be presented on those claims, the Bankruptcy Court entered an order on March 18, 1983 specifying that if Petitioners sought to pursue their claims, the claims should be made in the context of an adversary proceeding rather than by motion or application. Thereafter, Petitioners filed a complaint seeking substantially the same relief requested in the Application.

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[1] Petitioners filed a notice of appeal of the Court's order approving the sale. Petitioners did not request a stay of the order, and the appeal was dismissed for lack of prosecution.

A ten-day trial on the merits of the complaint was held before the Bankruptcy Court, Judge Russell B. Seymour presiding. Mr. Galardi, an experienced trial attorney, conducted the trial on behalf of Petitioners. No request for a jury trial was made by Petitioners in the application, the complaint, or at any time during the course of the trial.[2] The jurisdiction of the Bankruptcy Court was based upon the Emergency Rule for the Central District of California, promulgated after the stay of the *Marathon* decision expired.

The bankruptcy judge submitted findings of fact and conclusions of law, a Report and Recommendation, and a proposed judgment to the District Court. These documents were lodged more than seven weeks after the conclusion of the trial, and after the Bankruptcy Court had held the documents for one week to provide Petitioners an opportunity to file written objections.[3] The District Court signed the judgment on September 16, 1983, and the judgment was entered on September 26, 1983.

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[2] Petitioners failed to request a jury trial pursuant to Bankruptcy Rule 9015, and expressly stated at the commencement of trial that they had chosen to try the case before the judge without a jury. Further, no jury trial was required because the case was a "core proceeding" since Petitioners were challenging the method and manner of the trustee's liquidation of property of the Chapter 7 bankruptcy estate.

[3] At the conclusion of trial, Petitioners advised the Court that they would file objections to the proposed findings and conclusions and a memorandum of law in support of their position. They also acknowledged that they would have the right to file a motion seeking to amend any documents signed by the Court.

B. Issues Presented to the Court of Appeals and Affirmance of the District Court Judgment

The decision of the Ninth Circuit confirms that the claims asserted by Petitioners were "core" matters arising under the bankruptcy laws and that the Bankruptcy Court's exercise of jurisdiction over the proceeding was valid under the Emergency Rule since Petitioners sought equitable relief and challenged the Chapter 7 trustee's conduct in liquidating the estate. Petitioners therefore had no constitutional right to jury trial.

The Court further found that the District Court properly reviewed the proposed findings of fact and conclusions of law and entered judgment accordingly. The Court noted that Petitioners filed no objections to the findings, conclusions, and proposed judgment and held that the District Court therefore properly based its determination on the pleadings and papers which it had before it.

As to the issue of the appointment powers of the District Court, the Court found that the appointment was expressly authorized under the powers reserved to the District Court in Section 404(d) of the Bankruptcy Reform Act and Section 40(d)(2) of the Bankruptcy Act of 1898. Under the Bankruptcy Act of 1898, courts of bankruptcy are defined in Section 1(10) as the district courts, and Section 404(a) of the transition statutes continued the existing courts of bankruptcy under the former Bankruptcy Act until March 31, 1984.

The Court of Appeals also found full support in the record for the judgment and the findings that the auction sale was properly conducted in all respects and that it was Petitioners who attempted to disrupt the sale and cause confusion. For a more complete recitation of the underlying

facts of the case which details Petitioners' scheme to cloud title to the properties and discourage bidders at the auction sale, please see the procedural and factual history of the case from Respondent's brief submitted to the Court of Appeals for the Ninth Circuit, attached hereto as Appendix 1.

II

SUMMARY OF ARGUMENT IN OPPOSITION TO GRANT OF CERTIORARI.

The case at bar is nothing more than a routine bankruptcy proceeding in which the Chapter 7 debtors have objected to the Chapter 7 trustee's manner of liquidating property of the estate. The case presents no special questions of federal law, no unique facts, and no unsettled legal issues. To the contrary, the decision of the Court of Appeals affirming the judgment is based on substantial, well-settled and well-reasoned authority.

In this case, the Court of Appeals for the Ninth Circuit held that under the authority of *Katchen v. Landy*, 382 U.S. 323, 336-340 (1966), there is no constitutional right to a jury trial in a bankruptcy proceeding such as the core proceeding at issue. Moreover, Bankruptcy Rule 9015 provides a specific mechanism by which Petitioners could have requested a jury trial. No request for a jury trial was ever made by the Petitioners, and the transcript of the trial reveals an *express acknowledgment on the part of Mr. Galardi that he deliberately chose not to request a jury trial. See, Reporter's Transcript,* (hereinafter "R.T.") June 21, 1983, 62:23-63:2.

As to Petitioners' contention that the District Court failed to review the determination of the Bankruptcy Court, the District Court reviewed the findings of fact and conclusions of law, the report and recommendation and the proposed judgment. Petitioners made no objection to the proposed findings and judgment. Petitioners submitted no legal memoranda or other pleadings or additional evidence to the District Court or the Bankruptcy Court, and Petitioners made no request for a hearing before the District Court, despite Petitioners' attempts to suggest otherwise. *See*, Petition for Writ of Certiorari, page 17.

As to the appointment of a retired bankruptcy judge, the transition statutes of the Bankruptcy Reform Act of 1978 expressly provide that Section 40(d)(2) of the former Bankruptcy Act was to remain in effect through March 31, 1984. *See*, Section 404(d) of the Bankruptcy Reform Act of 1978. The transition statutes further provide that the courts of bankruptcy, defined as the district courts under Section 1(10) of the Bankruptcy Act of 1898, were to also remain in existence until March 31, 1984. Section 40(d) of the former Bankruptcy Act grants the District Court the authority to call upon retired bankruptcy referees to perform bankruptcy duties.

ARGUMENT

III

PETITIONERS WERE NOT DENIED THE RIGHT TO A JURY TRIAL.

Petitioners at no time requested a jury trial and made no reference to a request for a jury trial until final argument at the trial on July 18, 1983. Mr. Galardi, an experienced trial

attorney, was apparently fully aware of his rights and made a conscious decision to try the matter before Judge Seymour. That Petitioners knowingly and deliberately chose not to request a jury trial is clear from the record of the proceeding. As Mr. Galardi stated:

> We don't have a jury here. *I could have asked for a jury trial.* I am confident that you are going to sort the wheat from the chaff as my learned friend suggests. Every judge I have ever been before in my life has been able to do that. (Emphasis added.) R.T., June 21, 1983, 62:23-63:2.

Further, as the United States Court of Appeals for the Ninth Circuit noted, this case is clearly a core proceeding arising under the bankruptcy laws. The claims of Petitioners strike at the heart of a Chapter 7 proceeding by challenging the Chapter 7 trustee's actions in conducting the liquidation. The right of the Bankruptcy Court to exercise jurisdiction over such a "core" proceeding was held to be constitutional in the *Marathon* decision, and the Bankruptcy Court's power to adjudicate "core" proceedings was confirmed through the Emergency Rule for the Central District of California.

Since a Bankruptcy Court is a court in equity, there is no constitutional right to a jury trial. *See, Katchen v. Landy, supra.* Further, the relief sought by Petitioners in their complaint includes claims for declaratory and injunctive relief, matters in equity for which there is no right to a jury trial.

IV

THE DISTRICT COURT'S REVIEW WAS CONDUCTED IN ACCORDANCE WITH THE EMERGENCY RULE AND SATISFIED THE REQUIREMENTS OF DUE PROCESS OF LAW.

Petitioners argue that their due process rights were abridged either (1) by the Bankruptcy Court exercising jurisdiction over the proceeding regardless of whether the bankruptcy judge was supervised by the District Court, or (2) by the District Court allegedly failing to review the Bankruptcy Court's decision as a required under the *Marathon* decision and the Emergency Rule promulgated thereafter. Regardless of how Petitioners frame the alleged constitutional violation, their arguments have no merit and were properly rejected by the Ninth Circuit.

A. The Emergency Rule and the District Court Reference of the Adversary Proceeding Were Constitutional.

The adversary proceeding at issue was filed after the decision of this Court in *Northern Pipeline Construction Company v. Marathon Pipeline Company*, 458 U.S. 50 (1982), and after the stay of the *Marathon* decision had expired. The trial was held before the bankruptcy judge pursuant to the general order of reference contained in the Emergency Rule promulgated by the District Court for the Central District of California.

The Circuit Courts of Appeal which have been asked to decide the issue have consistently held that the *Marathon* decision had no effect on the grant of bankruptcy

jurisdiction to the district courts contained in 28 U.S.C. Section 1471(a) and 1471(b). *See, e.g., In re Thomas*, 765 F.2d 926, 929 (9th Cir. 1985); *In Re Kaiser*, 722 F.2d 1574, 1578 (2d Cir. 1983); *Oklahoma Health Services Federal Credit Union v. Webb*, 726 F.2d 624 (10th Cir. 1984); *White Motor Corp. v. Citibank*, N.A., 704 F.2d 254 (6th Cir. 1983); *In Re Hansen*, 702 F.2d 728, 729 (8th Cir. 1983); *In Re Braniff Airways, Inc.*, 700 F.2d 214 (5th Cir. 1983), *cert. denied*, 461 U.S. 944 (1983); *Accord, Coastal Steel Corporation v. Tilghman Wheelabrator, Ltd.*, 709 F.2d 190 (3d Cir. 1983).

The Court of Appeals for the Ninth Circuit has expressly upheld the constitutionality of the Emergency Rule for the Central District of California, and rules similar to this local Emergency Rule have also been consistently upheld by those courts which have dealt with the issue. *See, In re Thomas, supra; In Re Kaiser, supra, In Re Stewart*, 741 F.2d 127, 129 (7th Cir. 1984); *In Re Hansen, supra; Oklahoma Health Services, Etc. v. Webb, supra; White Motor Corp. v. Citibank, N.A., supra.* The power of the district court to promulgate rules necessary and appropriate for the conduct of its business, and thus to create the automatic reference of bankruptcy cases to the bankruptcy judges, is expressly established in 28 U.S.C. Section 2071. A copy of the Emergency Rule for the Central District of California is attached hereto as Appendix 2.

Although the proceeding at issue is clearly a "core" proceeding arising under the bankruptcy laws, out of an abundance of caution, the Bankruptcy Court submitted the findings of fact and conclusions of law, a report and recommendation, and a proposed judgment to the District

Court for review and entry of judgment.[4] The constitutionality of a bankruptcy judge making final determinations in "core" bankruptcy proceedings was not disputed by this Court in the *Marathon* decision. Nevertheless, even if, *arguendo*, the proceeding at issue was a "related" proceeding, the procedures followed by the Bankruptcy Court in referring the matter to the District Court for a final determination comport with both the spirit and the letter of the law under *Marathon*.

B. The District Court Properly Reviewed the Bankruptcy Court's Determination and Properly Entered Judgment in Favor of All the Defendants.

Petitioners make the unsupported assertion that the District Court did not adequately review the Bankruptcy Court's findings and proposed judgment in this case. Petitioners cite Rule (e)(2)(B) of the Emergency Rule for the Central District of California and properly acknowledge that the district judge has broad discretion in determining the manner in which his or her review will be conducted. *See*, Petition for Writ of Certiorari, page 17.

It has become a maxim of law that the concept of due process is flexible and requires only that procedural safeguards and opportunities appropriate to the nature of the case be provided. *See, e.g.* , *United States v. Raddatz*,

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[4] The Emergency Rule expressly provided that the bankruptcy judge in his discretion could submit findings, conclusions and a proposed judgment to the District Court for review and entry of a final order if the bankruptcy judge determined that procedure to be appropriate under the circumstances of the case. *See* Section (d)(3)(B) of the Emergency Rule.

447 U.S. 667 (1980); *Mathews v. Eldridge*, 424 U.S. 319 (1976). The right to due process does not permit a litigant to ignore the procedures available for review and later complain of a violation of his or her due process rights.

In the case at bar, almost seven weeks passed between the conclusion of the trial and the submission of the findings of fact and conclusions of law to the Bankruptcy Court. The Bankruptcy Court then held the findings and conclusions for an additional week to permit Petitioners to make objections or to submit their own proposed findings or other pleadings to the Court. Petitioners were fully aware of the procedures which the Court would employ and of their right to request a new trial or to seek to amend the judgment or findings. As Mr. Galardi stated on July 18, 1983 at the close of trial:

> Why don't we go ahead and have the findings and conclusions submitted by defendants, as the Court indicated it is inclined to rule in favor of defendants as represented by Mr. Graham? *And I'll have five days within which to submit counterproposed findings and conclusions.* The court may elect to adopt some of them. *And then under the Rules I have ten days within which to move to amend anything that the Court actually signs.*" (Emphasis added.) R.T. July 18, 1983, 194:6-14.

Petitioners took none of the steps available to them to attempt to modify the Bankruptcy Court's determinations or enhance the review by the District Court. Analogous cases have dealt with the *de novo* review of a magistrate's decision and the effect of a party's failure to take advantage of the opportunities available to the unsuccessful litigant. These cases stand for the proposition that Petitioners cannot

complain when they have failed to avail themselves of the procedures available. *See, e.g., Nettles v. Wainwright*, 677 F.2d 404, (5th Cir. 1982) ("[i]f a party has objections, it is essential that he apprise the district court").

The rationale for this rule was well-stated by the Court in the *Nettles* case:

> . . . no undue burden exists in requiring an attorney or a pro se litigant to state his objections, if any, to the district court. . . . Requiring them to assist the district court by stating their objections is a small order. *We will not sit idly by and observe the 'sandbagging' of district judges where an appellant fails to object to a magistrate's report in the district court and then undertakes to raise his objections for the first time in this court.* (Emphasis added.) *Id.* at 410.

When a party fails to object to the findings of a magistrate and when the district court adopts those findings and enters a judgment or an order in accordance therewith, no explanation or statement need be given by the district court to support its decision. As the Court of Appeals for the Fourth Circuit has stated:

> Adoption is an affirmative act. In the absence of objection, for which provision is made by the statute, we do not believe that it requires any explanation. *We also do not believe it may be presumed by the absence of explanation, as plaintiff requests us to do, that the judge who entered the order adopting the Magistrate's report had not given the report any consideration at all. Indeed, quite the contrary is true for official acts are presumed to be regular,* and since the judge had the power either to accept, reject, or

> modify the report in whole or in part, we will not consider that the judge did not exercise the discretion which the statute gives him." (Emphasis added.) *Camby v. Davis*, 718 F.2d 198, 198, 199 (4th Cir 1983).

The papers submitted to the District Court in this case consisted of more than 70 separate and detailed findings of fact and three pages of conclusions of law specifically addressing each of the legal issues raised by Petitioners. The District Court had before it more than enough information to be apprised of the nature of the lawsuit and the events of the trial.

The Court of Appeals for the Ninth Circuit specifically found that the district judge conducted an appropriate review in light of the failure of Petitioners to submit objections or any other pleadings or papers to the Bankruptcy Court or the District Court. The Ninth Circuit found that the district judge acted as the ultimate decision-maker, satisfying the requirements of due process and Article III of the Constitution. Petitioners' constitutional rights have been adequately safeguarded in light of the lengthy trial before the Bankruptcy Court and the full review of the case by both the District Court and the Court of Appeals.

V

THE DISTRICT COURT HAD AUTHORITY TO APPOINT JUDGE SEYMOUR TO SIT AS A BANKRUPTCY JUDGE.

Judge Seymour was appointed by the District Court pursuant to express statutory authority. Specifically,

Section 404(a) of the Bankruptcy Reform Act of 1978, Public Law 95-598, states in pertinent part:

> The courts of bankruptcy, as defined under Section 1(10) of the Bankruptcy Act, created under Section 2(a) of the Bankruptcy Act, and existing on September 30, 1979, shall continue through March 31, 1984, to be the courts of bankruptcy for the purposes of this Act and the amendments made by this Act.

Section 1(10) of the Bankruptcy Act defines "courts of bankruptcy" as the district courts. Thus, during the transition period, the powers of the district court concerning the administration of bankruptcy cases were to remain in effect as they had been under the Bankruptcy Act of 1898. *See also, Collier on Bankruptcy*, 15th Ed., Vol. 1, ¶ 2.01, pp. 2-12.

Section 404(d) of the Bankruptcy Reform Act of 1978 states that during the transition period, matters relating to bankruptcy judges shall continue to be governed by certain provisions of the Bankruptcy Act of 1898, including Section 40(d) of the Act. Section 40(d)(2) of the Act provides in pertinent part:

> Any referee who has retired or been retired under the provisions of paragraph (1) of this subdivision may, if called upon by a judge of a court of bankruptcy, perform such duties of a referee, conciliation commissioner, or special master under this Act, within the jurisdiction of the Court, as he may be able and willing to undertake.

The District Court, under the powers conferred by the Bankruptcy Act and the transition statutes, called upon Judge Seymour to serve as a bankruptcy judge. The order appointing Judge Seymour under the authority of the

above-cited statutes was made a part of the record on appeal.

VI

PETITIONERS HAVE RAISED NO CLAIMS TO JUSTIFY REVIEW ON CERTIORARI.

No important or special issue of law has been presented by Petitioners which would warrant this Court's grant of the Petition for Writ of Certiorari. To the contrary, the judgment of the District Court and the decision of the United States Court of Appeals for the Ninth Circuit affirming that judgment are firmly grounded in substantial, well-reasoned and well-settled law.

VII

CONCLUSION

For the reasons set forth herein, and based upon the foregoing arguments and authorities, Respondent respectfully submits that the Petition for Writ of Certiorari should be denied.

Dated: March 10, 1986

Respectfully submitted,

FRANDZEL & SHARE
A Law Corporation
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Attorneys for Respondent
TOKAI BANK OF CALIFORNIA

APPENDIX 1

No. 83-6385

IN THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

In re:
LAWRENCE J. GALARDI, a professional corporation, and SHARI J. GALARDI,
Debtors.

LAWRENCE J. GALARDI and SHARI J. GALARDI,
Plaintiffs-Appellants,
vs.
TOKAI BANK OF CALIFORNIA, a California corporation, et al.,
Defendants-Appellees.

APPELLEE'S BRIEF

I

STATEMENT OF THE CASE

The litigation arises out of an auction sale of two parcels of real property which had been property of the appellants' bankruptcy estate. The auction sale was conducted by the Chapter 7 bankruptcy trustee pursuant to a November 24,

1982 order of the bankruptcy court approving the sale. This appeal represents the final chapter in the saga of appellants' improper efforts to thwart the bankruptcy trustee's sale of the properties.

The appellants' sought to set aside the auction sale by filing a complaint for declaratory and injunctive relief in the bankruptcy court. The complaint alleged that the bankruptcy court did not have jurisdiction over the subject matter raised in the complaint, that the auction sale conducted pursuant to the court order was illegal and void, that the appellees violated the automatic stay of 11 U.S.C. § 362 by conducting the auction, and that an injunction should issue restraining the appellees, including the trustee, from taking possession or otherwise disposing of the two parcels of real property. On appeal, appellants have apparently waived their request for the above-described relief and have requested only that this Court remand the case for trial on the issue of damages allegedly resulting from the trustee's sale of one of the two real properties. (Appellants' Opening Brief, pp. 6, 45, 46.)

A. Procedural History Of The Case

Appellants Lawrence and Shari Galardi filed their petition under Chapter 11 of the Bankruptcy Code on January 20, 1981, Bankruptcy Case Number LA 81-00606. On October 1, 1981, an order was entered directing the appointment of a trustee and David A. Gill, an appellee herein, was so appointed. The Chapter 11 proceeding was subsequently converted to a Chapter 7 liquidation proceeding on July 23, 1982, and David A. Gill was appointed as trustee of the Chapter 7 estate. (Appellants' Appendix, Vol. II, p. 346, hereinafter "App.".)

The assets of appellants' Chapter 7 bankruptcy estate included two parcels of real property known as the Cool Oak Way property (also known as the 29 acres property) and the Eagle Pass property. Appellee Tokai Bank was the holder of first position deeds of trust on each of the two properties. Defendant Cambridge Capital Group was the holder of a second deed of trust on the Eagle Pass property.[1] (App., Vol. II, pp. 243-249.)

1. The Order Approving the Auction Sale

On October 18, 1982, Tokai Bank and the trustee filed a joint application to conduct a public auction sale of the two properties. (App., Vol. II, p. 346.) On November 24, 1982, the bankruptcy court entered an order granting the application and directing that the two properties be sold. The order further provided that the trustee was authorized to employ Marsh Dozar as the auctioneer and approved Tokai Bank's allowed secured claim. The order also approved Tokai Bank's minimum credit bid for the Cool Oak Way property and approved the terms for a qualified buyer to make a financed bid. (App., Vol. II, p. 347.)

Appellants subsequently appealed the court's November 24, 1982 order to the Bankruptcy Appellate Panel on December 13, 1982, one day after the auction sale was conducted. Appellants at no time sought a stay of the order. Appellants failed to prosecute that appeal, and the appeal was dismissed on December 6, 1983. (App., Vol. II, p. 350.)

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[1] Cambridge Capital Group was dismissed from this appeal by appellants. (Appellants' Opening Brief, p. 2, fn. 2.)

2. The Intervening Bankruptcy of Heatherfield Interiors

On December 9, 1982, three days prior to the scheduled auction sale, appellant Shari Galardi created Heatherfield Interiors, Inc., a California corporation. The debtor Shari Galardi was the sole shareholder of that corporation. On the same date that Heatherfield Interiors, Inc. was incorporated, Shari Galardi purportedly transferred all of her right, title and interest in the Cool Oak Way and Eagle Pass properties to the corporation. (App., Vol. II, pp. 246-247.)

This "transfer" of assets of the Galardi bankruptcy estate was made without the knowledge or consent of the bankruptcy trustee or the bankruptcy court. (App., Vol. II, p. 247.) On the following day, December 10, 1982, Heatherfield Interiors, Inc. filed a petition under Chapter 11 of the Bankruptcy Code, listing the two parcels of real property as assets of Heatherfield despite the fact that title to the properties had been vested in the Galardis' bankruptcy estate for almost two years. (App., Vol. II, pp. 241-252.)

The "claim" of Heatherfield Interiors, Inc. to the Cool Oak Way and Eagle Pass properties was the subject of an adversary proceeding commenced by Heatherfield Interiors, Inc. against Cambridge Capital Group, Tokai Bank and others. *Heatherfield Interiors, Inc. v. Cambridge Capital Group, etc., et al.*, Adv. No. LA 83-2003 RS. The matter was tried before Bankruptcy Judge Russell B. Seymour. (App., Vol. II, pp. 237-239.) A judgment was entered against appellants and in favor of all defendants in that action, and the findings of fact and conclusions of law, the report and recommendation, certification for review,

and judgment in that proceeding were admitted into evidence in the trial on this matter. (App., Vol. II, pp. 233-252, Def. Ex. 107-109.)

The auction sale of the real properties was conducted on December 12, 1982. The Cool Oak Way property was sold to Tokai Bank at the price previously approved by the bankruptcy court because no other bids were made on the property. The sale of the Eagle Pass property was conducted *with reserve* pursuant to the court's prior order. (App., Vol. I, pp. 49-55.) The highest bid for the Eagle Pass property was $1 million; however, at least $1.5 million dollars was needed to pay the allowed secured claims of Tokai Bank and Cambridge Capital Group. Because a $1 million bid was insufficient to pay the liens on the property, the $1 million bid was rejected by the trustee's attorney. (Def. Ex. 100.)

3: The Adversary Proceeding

On January 20, 1983, appellants filed an application requesting relief similar to that prayed for in the subject adversary proceeding. (App., Vol. II, p. 348.) Because of the evidentiary nature of the dispute, the bankruptcy court converted the matter to an adversary proceeding pursuant to Bankruptcy Rule 9014. The order dismissing the application was signed by the court on March 18, 1983. (App., Vol. I, p 89; App., Vol. II, p. 348.) Thereafter, appellants filed their complaint for declaratory and injunctive relief, which adversary proceeding is the subject of this appeal.

The bankruptcy court's jurisdiction over the adversary proceeding was based on the Emergency Rule for the Central District of California, promulgated after the stay of

the *Marathon* decision expired. The bankruptcy judge made findings of facts and conclusions of law, a report and recommendation, and a proposed judgment was referred the matter to the district court. Judgment was entered on September 26, 1983 and notice of appeal was filed on October 24, 1983. (App., Vol. I, pp. 1, 26.)

B. Factual History Of The Case

The subject properties are located in Malibu, California. The Cool Oak Way property consists of 28.71 acres of undeveloped land. (Pl. Ex. 7.) The Eagle Pass property is comprised of 8 acres of land with a partially completed large Tudor-style mansion. (Pl. Ex. 7.) Mr. and Mrs. Galardi were the vested owners of the Cool Oak Way property and Lawrence Galardi was the vested owner of the Eagle Pass property. (App., Vol. II, p. 243.)

Appellee Tokai Bank was the construction lender for the large, Tudor-style mansion on the Eagle Pass property.[2] The construction project suffered set-backs and cost overruns, and the Galardis ultimately filed a petition in bankruptcy.

The Eagle Pass and Cool Oak Way properties were the primary assets of the Galardi bankruptcy estate. After 18 months, the reorganization proceeding was unsuccessful and the proceeding was converted to a Chapter 7 case. The Chapter 7 trustee then proceeded to liquidate the assets of the Galardis' estate.

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[2] Plaintiffs' Exhibit 17, the loan documents on these properties, was admitted into evidence at trialand isone of the exhibits which was lost. (App., Vol. II, pp. 243-244.)

The trustee and the primary lien holders on the properties entered into stipulations to provide for an orderly sale of the properties. (App., Vol. II, pp. 272-276, pp. 213-216.) The letter agreement between Tokai Bank and the trustee, dated October 8, 1982 (Def. Ex. 103), provided for a $641,000.00 minimum credit bid on the Cool Oak Way property and Tokai Bank guaranteed the payment of certain auction expenses and commissions. In addition, Tokai Bank offered financing to 243-244.) prospective purchasers.[3] The Court ultimately approved the auction sale of the properties pursuant to its order of November 24, 1982. (Pl. Ex. 1.)

1. Pre-Auction Maneuvers and the Creation of Heatherfield Interiors, Inc.

One week prior to the scheduled auction, appellants presented to the attorney for the trustee an offer to purchase the properties.[4] This offer, which was contingent

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[3] This October 8, 1982 letter agreement is also known as the "confidential letter agreement". Appellants have placed before this Court an inaccurate copy of the letter agreement with the words "in error" in Mr. Galardi's handwriting. (Pl. Ex. 6; App., Vol. II, pp. 184-192.) This exhibit was excluded when defendant produced the original letter, Defendant's Exhibit 103. (R.T., June 27, 1983, pp. 1-3.) Copies of the letter agreement were distributed to the interested parties at the hearing on the application to approve the auction sale, but the agreement was otherwise kept confidential to encourage competitive bidding by not disclosing to the public the minimum acceptable bids. [R.T., June 23, 1983, p. 24, lines 4-8.]

[4] This offer, Plaintiffs' Exhibit 13, named Douglas Blankenship, the Galardis' alleged partner, as the sole purchaser and was signed by Kenneth Hardin, purportedly as agent for Mr. Blankenship. (App., Vol. II, pp. 208-209.) In his testimony at trial, Mr. Blankenship denied that there was a partnership between he and the Galardis and denied that

upon obtaining financing and did not include an earnest money deposit, was rejected by the attorneys for the trustee (R.T., June 24, 1983, page 168, lines 11-17; June 30, 1983, page 116, lines 21-24.)

The Galardis then implemented a thinly-veiled scheme to cloud title to the properties and to discourage bidders at the auction sale. On December 9, 1982, three days before the scheduled auction sale, Shari Galardi incorporated an entity known as Heatherfield Interiors, Inc., a California corporation. On the same date, Shari Galardi purported to transfer the Cool Oak Way property and the Eagle Pass property from the Galardi bankruptcy estate to Heatherfield Interiors, Inc.

On December 10, 1982, at 4:07 p.m., the entity Heatherfield Interiors, Inc. filed a Chapter 11 petition in bankruptcy and scheduled the Cool Oak Way and Eagle Pass properties as assets of the Heatherfield bankruptcy estate. (Def. Ex. 109; Def. Ex. 101.) The sham nature of the corporation and its alleged interest in the Cool Oak Way and Eagle Pass properties were fully proven in the Heatherfield adversary proceeding. The judgment in that proceeding is final and no appeal was ever taken from that judgment.

The findings of fact and conclusions of law which were admitted into evidence at trial conclusively determined that the subject properties had at all times been property of the Galardi bankruptcy estate, and that the purported transfer to Heatherfield Interiors was made without the knowledge or consent of the trustee or the bankruptcy court. (Def. Ex.

Mr. Hardin had authority to submit the purchase offer (R.T. June 30, 1983, p. 170, lines 22-25, p. 171, line 1, p. 174, lines 2-13, p. 190, p. 175, lines 2-20.)

109, App. Vol. II, pp. 241-252; R.T., June 29, 1983, p. 75, lines 5-19, p. 76, lines 5-9, pp. 204-105.)

2. Appellants' Activities at the Auction Sale

In an effort to confuse the bidders and forestall the auction, appellants posted notices of the Heatherfield bankruptcy filing in several obvious locations around the Eagle Pass property on the day the auction was to take place. Specifically, appellants posted notices stating that Heatherfield Interiors, Inc. had an interest in the Cool Oak Way and Eagle Pass properties, that Heatherfield had filed a Chapter 11 petition, and that the automatic stay of 11 U.S.C. § 362 prohibited the sale or other disposition of any Heatherfield property. (Def. Ex. 101; R.T., June 29, 1983, p. 73, line 25, p. 74, lines 1-20.)

Mr. Galardi specifically requested that the auction sale be cancelled (R.T., June 23, 1983, p. 18, lines 20-24). When Leslie Cohen, one of the attorneys for the trustee, attempted to remove the Heatherfield notices, Mr. Galardi admonished her not to remove them. When she did remove them, Mr. Galardi called the county sheriff in a further attempt to create confusion and disrupt the sale (R.T., June 24, 1983, p. 184, lines 6-25, p. 185, lines 2-10). When Bennett Silverman, the attorney for Cambridge Capital Group, attempted to remove one of the notices, a friend of the Galardis attempted to restrain him from doing so (R.T., July 12, 1983, p. 38, lines 10-25, p. 39, lines 1-21.)

A good friend of the Galardis, John Corrodi, arrived at the auction with his seven children with no intention to bid (R.T., June 22, 1983, pp. 46-47). Although Mr. Corrodi was not a qualified bidder and had indicated to the auctioneers

that he was not there to bid, Mr. Corrodi attempted to disrupt the auction by questioning the auctioneers regarding the Heatherfield bankruptcy. (R.T., June 23, 1983, p. 3; June 24, 1983, p. 182 lines 3-10.)[5]

3. The Auction Sale

The tape recording of the auction sale, Defendant's Exhibit 100, demonstrates that numerous attempts were made to obtain bids from the public. The property was offered on both a cash and a terms basis in accordance with the court order. (R.T., June 23, 1983, p. 50, lines 17-23.) After waiting for several minutes and attempting to obtain a bid, the auctioneer sold the property to Tokai Bank at the court-approved price. (R.T., June 24, 1983, p. 96, lines 5-19.) Some months later, Tokai Bank resold the Cool Oak Way property to Donald L. Lewis. (App., Vol. II, p. 183.)

The autcioneers then proceeded to auction the Eagle Pass property *with reserve.* Bidding opened at $1 million cash and Douglas Blankenship, the alleged partner of Galardi, made a bid in that amount (R.T., June 24, 1983, p. 19, lines 3-9, lines 15-19.) No bids in a higher amount were received, and the attorney for the trustee rejected the $1 million bid since it was insufficient to pay the allowed secured claims of Tokai Bank and Cambridge Capital Group.

Bidding was opened on a financed basis and again Blankenship bid $1 million. The trustee rejected that bid and indicated that a bid of at least $1.5 million was required

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[5] Mr.Corrodi was aware of the Heatherfield matter since he had discussed the Heatherfield filing with the attorney who filed the Heatherfield bankruptcy petition and was present at the attorney's office at the time the Galardis were there. (R.T., June 22, 1983, p. 72, lines 3-18, p. 73, lines 9-16.)

to satisfy prior liens on the property. No further bids were forthcoming. (Def. Ex. 100; R.T., June 24, 1983, p. 171, lines 8-13, p. 172, lines 18-21, p. 124, lines 14-25, p. 125, lines 1-25, p. 126, lines 1-4; July 12, 1983, p. 34, lines 9-25, p. 35, lines 1-17, p. 36, lines 3-8.)

4. Post-Auction Litigation

Arguing that the auction sale was "confusing" and that bidding was somehow precluded, appellants challenged the conduct of the auction in the pending litigation.[6]

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[6] Appellants only called three independent witnesses to support their claim of "confusion" and "unfairness" although there were approximately 85 people at the auction, most of whom were friends of the Galardis. (R.T., June 29, 1983, p. 71, lines 18-25.) The strength and credibility of the witnesses' testimony will be discussed in detail in the latter portions of this brief.

APPENDIX 2

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

LOCAL RULE GOVERNING BANKRUPTCY CASES AND PROCEEDINGS

(a) Emergency Resolution

The purpose of this rule is to supplement existing law and rules in respect to the authority of bankruptcy judges of this district to act in bankruptcy cases and proceedings until Congress enacts appropriate remedial legislation in response to the Supreme Court's decision in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, __U.S__, 102 S.Ct. 2858 (1982), or until March 31, 1984, whichever first occurs.

The judges of the District Court find that exceptional circumstances exist. These circumstances include: (1) the unanticipated unconstitutionality of the grant of power to bankruptcy judges in Section 241(a) of the Bankruptcy Act of 1978; (2) the clear intent of Congress to refer bankruptcy matters to bankruptcy judges; (3) the specialized expertise necessary to the determination of bankruptcy matters; and (4) the administrative difficulty of the District Court's assuming the existing bankruptcy caseload on short notice.

Therefore, the orderly conduct of the business of the court requires this referral of bankruptcy cases to the bankruptcy judges.

(b) Filing of bankruptcy papers

Bankruptcy cases and related proceedings shall be filed with the Bankruptcy Clerk and assigned to bankruptcy judges, including those matters to be reviewed by a District Court Judge.

In all pleadings after referral by a bankruptcy judge to a District Court Judge, the caption shall contain the following notice: "REFERRED TO U.S. DISTRICT COURT".

The court of bankruptcy constituted by Section 404 of the Bankruptcy Act of 1978 shall continue to be known as the United States Bankruptcy Court of this district. The Clerk of the Bankruptcy Court is hereby designated to maintain all files in bankruptcy cases and adversary proceedings. All papers in cases or proceedings arising under or related to Title 11 shall be filed with the Clerk of the Bankruptcy Court regardless of whether the case or proceeding is before a bankruptcy judge or a judge of the District Court, except that a judgment by the District Judge shall be filed in accordance with Rule 921 of the Bankruptcy Rules. Upon reference to a United States District Judge the moving party shall give notice to affected parties, advising them of the requirement that subsequent pleadings shall identify the District Judge to whom the matter has been referred.

The moving party shall also provide the District Court with a list of the names and addresses of all parties served.

In any matter to be heard before a District Judge under these Rules, the Local Rules of the District Court must be strictly complied with, including the requirement that documents presented for filing must be accompanied by a legible copy for the use by the District Judge. The Clerk of the Bankruptcy Court is authorized to reject any filing which does not comply with the requirement of this Local Rule.

(c) Reference to Bankruptcy Judges

(1) All cases under Title 11 and all civil proceedings arising under Title 11 or arising in or related to cases under

Title 11 are referred to the bankruptcy judges of this district.

(2) The reference to a bankruptcy judge may be withdrawn at any time by the District Court on its own motion or on timely motion by a party. A motion for withdrawal of reference shall not stay any bankruptcy matter pending before a bankruptcy judge unless a specific stay is issued by the District Court. If a reference is withdrawn, the District Court may retain the entire matter, may refer part of the matter back to the bankruptcy judge, or may refer the entire matter back to the bankruptcy judge with instructions specifying the powers and functions that the bankruptcy judge may exercise. Any matter in which the reference is withdrawn shall be reassigned to a District Judge in accordance with the court's usual system for assigning civil cases.

(d) Powers of Bankruptcy Judges

(1) The bankruptcy judges may perform in referred bankruptcy cases and proceedings all acts and duties necessary for the handling of those cases and proceedings except that the bankruptcy judges may not conduct:

(A) a proceeding to enjoin a court;

(B) a proceeding to punish a criminal contempt —

(i) not committed in the bankruptcy judge's actual presence; or

(ii) warranting a punishment of imprisonment;

(C) an appeal from a judgment, order, decree, or decision of a United States bankruptcy judge; or

(D) jury trials.

Those matters which may not be performed by a bankruptcy judge shall be transferred to a District Judge.

(2) Except as provided in (d)(3), orders and judgments of bankruptcy judges shall be effective upon entry by the Clerk of the Bankruptcy Court, unless stayed by the bankruptcy judge or a District Judge.

(3) (A) Related proceedings are those civil proceedings that, in the absence of a petition in bankruptcy, could have been brought in a District Court or a state court. Related proceedings include, but are not limited to, claims brought by the estate against parties who have not filed claims against the estate. Related proceedings do not include: contested and uncontested matters concerning the administration of the estate; allowance of and objection to claims against the estate; proceedings to lift the automatic stay; counterclaims by the estate in whatever amount against persons filing claims against the estate; proceedings to set aside preferences and fraudulent conveyances; orders to turn over property of the estate; orders authorizing use of cash collateral; orders approving the sale of property of the estate free and clear of liens; allowance or denial of discharge; proceedings to determine the dischargeability of a debt; proceedings regarding the confirmation of a plan; and similar matters. A proceeding is not a related proceeding merely because the outcome wil be affected by state law.

(B) In related proceedings, and wherever the bankruptcy judge determines that circumstances require that a judgment or order be entered by a District Judge, the bankruptcy judge shall not enter a judgment or dispositive order, but shall submit findings, conclusions, and a proposed judgment or order to the District Judge, unless the parties to the proceeding consent to entry of judgment or order by the bankruptcy judge.

(e) District Court Review

(1) A notice of appeal from a final order or judgment or proposed order or judgment of a bankruptcy judge or an application for leave to appeal an interlocutory order of a bankruptcy judge, shall be filed within ten (10) days of the date of entry of the judgment or order or of the lodgment of the proposed judgment or order. Modification by the District Judge or the bankruptcy judge of time for appeal is governed by Rule 802 of the Bankruptcy Rules. The procedures set forth in Part VIII of the Bankruptcy Rules apply to appeals of bankruptcy judges' judgments and orders except that:

(A) The provisions of Sections (e)(2)(A) and (e)(2)(B) of this rule shall apply;

(B) The procedural modifications set forth in Bankruptcy Interim Rule 8004 shall apply pertaining to applications for leave to appeal interlocutory orders; and

(C) The form and contents of record on appeal shall comply with Rules 4(b) and 9(a) and (b) of the Rules of the United States Bankruptcy Appellate Panels of the Ninth Circuit.

(2) (A) A District Judge shall review:

(i) an order or final judgment entered under Section (d)(2) if a timely notice of appeal has been filed or if a timely application for leave to appeal has been granted;

(ii) an order or final judgment entered under Section (d)(2) if the bankruptcy judge certifies that circumstances require that the order or judgment be approved by a District Judge, whether or not the matter was controverted before the bankruptcy judge or any notice of appeal or application for leave to appeal was filed; and

(iii) a proposed order or judgment lodged under Section (d)(3), whether or not any notice of appeal or application for leave to appeal has been filed.

(B) In conducting review, the District Judge may hold a hearing and may receive such evidence as appropriate and may accept, reject, or modify, in whole or in part, the order or judgment or proposed order or judgment of the bankruptcy judge, and need give no deference to the findings of the bankruptcy judge. At the conclusion of the review, the District Judge shall enter an appropriate order or judgment.

(3) When the bankruptcy judge certifies that circumstances require immediate review by a District Judge of any matter subject to review under Section (e)(2), the District Judge shall review the matter and enter an order or judgment as soon as possible.

(4) It shall be the burden of the parties to raise prior to the time of the entry of the order or judgment of the District Judge after review the issue whether the bankruptcy judge should have entered a proposed judgment or order under Section (d)(3) rather than an order under Section (d)(2).

(5) The provisions of 11 U.S.C. § 363(m) and § 364(e) are incorporated by reference into these rules to apply to any action taken in good faith pursuant to an order of the bankruptcy judges.

(f) Local Rules

In proceedings before a bankruptcy judge the Local Rules of the Bankruptcy Court shall apply. In proceedings before a District Judge, the Local Rules of the District Court shall apply.

(g) Bankruptcy Rules and Title IV of the Bankruptcy Act

Courts of bankruptcy and procedure in bankruptcy shall continue to be governed by Title IV of the Bankruptcy Act of 1978 as amended and by the Bankruptcy Rules prescribed by the Supreme Court of the United States pursuant to 28 U.S.C. § 2075 and limited by Section 405(d) of the Act, to the extent that such Title and Rules are not inconsistent with this rule and the holding of *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, __U.S__, 102 S.Ct. 2858 (1982).

(h) Effective Date and Pending Cases

This rule shall become effective December 25, 1982, and shall apply to all bankruptcy cases and proceedings not governed by the Bankruptcy Act of 1898, as amended, and filed on or after October 1, 1979. Any bankruptcy matters pending before a bankruptcy judge on December 25, 1982 shall be deemed referred to that judge.

I. Preliminary Matters

1. *Emergency Resolution* [(a)]

The purpose of this rule is to supplement existing law and rules in respect to the authority of bankruptcy judges of this district to act in bankruptcy cases and proceedings until Congress enacts appropriate remedial legislation in response to the Supreme Court's decision in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, __U.S__, 102 S.Ct. 2858 (1982), or until March 31, 1984, whichever first occurs.

The judges of the District Court find that exceptional circumstances exist. These circumstances include: (1) the unanticipated unconstitutionality of the grant of power of bankruptcy judges in Section 241(a) of the Bankruptcy Act of 1978; (2) the clear intent of Congress to refer bankruptcy

matters to bankruptcy judges; (3) the specialized expertise necessary to the determination of bankruptcy matters; and (4) the administrative difficulty of the District Court's assuming the existing bankruptcy caseload on short notice.

Therefore, the orderly conduct of the business of the court requires this referral of bankruptcy cases to the bankruptcy judges.

2. *The Bankruptcy Court is Alive and Well* [(b) 3rd ¶]

The court of bankruptcy constituted by Section 404 of the Bankruptcy Act of 1978 shall continue to be known as the United States Bankruptcy Court of this district.